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UNIVERSITY OF ALBERTA

A CRITICAL APPRAISAL OF THE MODES OF ACQUISITION OF OIL RIGHTS IN NIGERIA

BY

LAWRENCE ASEKOME ATSEGBUA ©

A thesis submitted to the Faculty of Graduate Studies and Research in partial fulfilment of the requirements for the degree of **MASTER OF LAWS**.

FACULTY OF LAW
Edmonton, Alberta
FALL 1992

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FACULTY OF GRADUATE STUDIES AND RESEARCH

The undersigned certify that they have read, and recommended to the Faculty of Graduate Studies and Research for acceptance, a thesis entitled "**A Critical Appraisal of the Modes of Acquisition of Oil Rights in Nigeria**" submitted by Lawrence Asekome Atsegbua in partial fulfilment of the requirements for the degree of Master of Laws.

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Linda Reif

Professor Linda Reif

Fred Judson

Professor Fred Judson

Date 26th August 1992

"Not by might, nor by power, but by the spirit...." Zechariah 4: 6.

Dedicated to my parents, my brother Felix, Stella and Portia. For their love, support and encouragement.

Abstract

Nigeria's oil industry is by far the most dynamic industry in Nigeria and the development of oil resources is the most significant economic event in recent years. The importance of oil to Nigeria's economy cannot, therefore, be overemphasised. Over the past twenty years, crude oil has become the single most important raw material in Nigeria's trade both in volume and in value and contributes over ninety per cent (90%) of Nigeria's foreign exchange earnings.

It is most appropriate, therefore, that a critical appraisal be made of the modes of acquisition of oil rights in Nigeria. Such an appraisal could serve several useful purposes: it could confirm or deny whether the changes that took place in the modes of acquisition of oil rights in Nigeria between 1969 and 1973 had resulted in *de facto* control of the oil industry by Nigerians; it could assist in determining whether the present modes of acquisition of oil rights in Nigeria are compatible with the principle of permanent sovereignty over natural resources; and it could also make recommendations as to how any shortcomings could be corrected.

This thesis takes a fresh look at a number of old and persistent problems, but unlike previous writings in this area, it not only records, but also analyzes the reasons for the fundamental changes which occurred in the modes of acquisition of oil rights in Nigeria between 1969 and 1973. In addition, this thesis examines whether there is any correlation between these new modes of acquisition of oil rights and the ultimate objectives of the government.

The first chapter is devoted primarily to the history of Nigeria's oil

industry and the modes of acquisition of oil rights before 1969. In the second chapter, the modes of acquisition of oil rights under the *Petroleum Act* of 1969 and equity participation are examined. In chapter three, we examine the modes of acquisition of oil rights under contractual joint ventures, while in chapter four the contribution of the principle of permanent sovereignty over natural resources to the modes of acquisition of oil rights is examined. Chapter five is the conclusion.

Preface

No commodity plays a more vital role than oil in the economy of the developing countries of the world. For a nation with enormous oil deposits such as Nigeria, oil is the basis of economic life. Oil exports provide not only a large share of national income, but are also the main foreign exchange earner. Oil, thus, represents a great asset which could potentially provide all the capital necessary for Nigeria's economic development.

This thesis is, therefore, inspired by the role the oil industry plays in Nigeria's economy. Between 1973 and 1991, the oil industry in Nigeria has contributed over ninety per cent (90%) of Nigeria's foreign exchange earnings. With a daily average production of 2 million barrels of oil, Nigeria is Africa's largest producer of oil and one of the world's largest exporters.

A further justification for this thesis arises from the fact that no analytical literature has recently been written on the modes of acquisition of oil rights in Nigeria. No existing work deals comprehensively with the complex political and economic issues of how *de facto* control of the oil industry could be achieved by Nigerians within the existing framework of the modes of acquisition of oil rights.

This thesis, therefore, attempts to transcend the existing literature on the modes of acquisition of oil rights in Nigeria. This thesis not only records but also analyzes the modes of acquisition of oil rights in Nigeria. It will be argued that despite the fundamental changes which took place in the modes of acquisition of oil rights in Nigeria, *de facto* control is in the hands of the international oil companies (IOCs), which are vertically integrated and carry out operations (upstream and downstream) in several countries.

It will also be argued that, in the absence of *de facto* control of the oil industry by Nigerians, it is highly doubtful whether the modes of acquisition of oil rights are compatible with the principle of permanent sovereignty over natural resources. The reasons for the fundamental changes which took place in the modes of acquisition of oil rights in Nigeria's oil industry are also examined.

It must be stressed at the outset that the aim of this thesis is not to make a case against the modes of acquisition of oil rights. It is only intended to point out some of the drawbacks in the modes of acquisition of oil rights which may undermine the attainment by the government of its objective of ultimately controlling the oil industry. In order for the government to achieve this, oil agreements with the IOCs must no longer be viewed simply as contracts, but as economic development agreements. Economic development agreements are agreements whereby a state engages the capital and technology of a foreign company, usually of one or more developed countries, in an undertaking designed to have a decisive positive impact on the developing country's economic development.

Economic development agreements will bring to the fore the development issue of the training of Nigerian personnel in technological and managerial skills of the oil industry. In addition, the employment of skilled Nigerian personnel in the oil industry, would go a long way in assisting the government in achieving *de facto* control of the oil industry.

Acknowledgement

I must acknowledge with a deep sense of gratitude, my indebtedness to my supervisor Professor David Percy for his able guidance and supervision in writing this thesis. Without his valuable criticisms and encouragement it would not have been possible for me to complete this thesis in record time.

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Table of Contents

Chapter 1

1.0. Introduction 1

1.1. The World Oil Industry in Retrospect 2

1.2. Nigeria's Role in the World Oil Industry 5

1.3. The History of Oil in Nigeria. 7

  1.3.a. The Appearance of Competitors 11

  1.3.b. The Acquisition of Oil Rights before 1969 12

    1.3.b.i. Oil Exploration Licence (OEL) 14

    1.3.b.ii. Oil Prospecting Licence (OPL) 14

    1.3.b.iii. Oil Mining Lease (OML) 16

  1.3.c. Subsequent Developments 19

    1.3.c.i. The Influence of the United Nations 22

    1.3.c.ii. The Influence of the Organization of Petroleum Exporting Countries (OPEC) 23

  1.3.d. An Assessment 25

Chapter 2

ACQUISITION OF OIL RIGHTS UNDER THE PETROLEUM ACT OF 1969

2.0. Introduction 28

2.1. The Background to the Act 28

2.2. Acquisition of Oil Rights under the Act 33

2.2.a. Oil Exploration Licence (OEL) 33

2.2.b. Oil Prospecting Licence (OPL) 34

2.2.c. Oil Mining Lease (OML) 35

2.2.d. Rights and Powers of holders of OPLs and OMLs .. 39

2.2.e. Assignment of an OPL or OML 41

2.2.f. Revocation of an OPL or OML 44

2.2.g. A Comparison of the pre-1969 Grants with Grants made under the Act 47

2.2.h. The Nature of the Interest Granted under the Act ... 51

2.3. Equity Participation 52

2.3.a. The Participation Agreement 58

2.3.b. The Operating Agreement 58

2.3.c. The Memorandum of Understanding (MOU) 59

2.3.d. The Heads of Agreements 60

2.3.e. An Assessment 60

Chapter 3

ACQUISITION OF OIL RIGHTS UNDER CONTRACTUAL JOINT VENTURES

3.0. Introduction 72

3.1. Choice of Legal Framework 73

3.1.a. The "Fixed Content System" 73

3.1.b. The "Agreement System" 76

3.1.c. The "Flexible System" (or Hybrid System) 76

3.2. Contractual Joint Ventures 79

3.2.a. The Production Sharing Contract (PSC) 79

3.2.b. The Nigerian Production Sharing Contract (PSC) ... 81

3.2.b.i. Rights and Obligations of AON under the PSC 81

(a) Operating Costs 82

(b) Reimbursement of AON's Operating Costs and Sharing of Profits 82

(c) Payment of Taxes 84

(d) Control and Management of Operations 85

(e) Work Programme and Expenditure 86

(f) Marketing of Available Oil 87

(g) Training of Nigerians 88

3.2.b.ii. An Assessment 94

3.2.c. The Service Contracts (SCs) 100

3.2.d. The Nigerian Service Contracts (SCs) 102

3.2.d.i. Rights and Obligations of the IOC

(Contractor) 102

(a) The Provision of Funds 102

(b) Reimbursement and Remuneration 103

(c) Payment of Taxes 104

(d) Training of Nigerians 105

(e) Exploration Programme and Budget 106

3.2.d.ii. An Assessment 107

3.2.e. Conclusion 110

3.3. Contractual Stability 112

3.3.a. Stabilization Clauses 113

3.3.b. Renegotiation Clauses 119

Chapter 4

THE PRINCIPLE OF PERMANENT SOVEREIGNTY OVER NATURAL RESOURCES AND ITS CONTRIBUTION TO THE MODES OF ACQUISITION OF OIL RIGHTS

4.0. Introduction 125

4.1. The Origin and Development 126

4.2. The Legal Status of the Resolutions 135

4.3. The Contribution of the Principle and its Compatibility with the Modes of Acquisition of Oil Rights 139

4.4. An Assessment 145

4.5. Conclusion 147

Chapter 5

5.0. General Conclusion and Recommendations 149

5.1. Nationalization of the Oil Industry 153

5.2. The Role of Indigenous Oil Companies in the Exploration and Production of Oil in Nigeria 154

Bibliography 158

Vita 173

Chapter 1

1.0. Introduction

The main purpose of this chapter is to trace the history of Nigeria's oil industry. In order to achieve this purpose, a framework of analysis will be constructed so as to facilitate an understanding of what has already taken place in the oil industry. This chapter is, therefore, divided into three sections.

In section one, we shall examine the changes which took place in the world oil industry between 1960 and 1970. As will become evident, Nigeria as a producer and exporter of oil was also affected by these changes. The second section is devoted to Nigeria's role in the world oil industry, while section three traces the history of Nigeria's oil industry and also examines the different modes of acquisition of oil rights before 1969. In addition, the reasons for subsequent developments which occurred in Nigeria's oil industry are examined.

This chapter thus lays the foundation for the discussion of the different modes of acquisition of oil rights under the *Petroleum Act* of 1969 and contractual joint ventures, which comprises the heart of this thesis and will be undertaken in chapters 2 and 3 respectively. It will be argued in chapter 4 that the modes of acquisition of oil rights in Nigeria are not compatible with the principle of permanent sovereignty over natural resources. Finally in chapter 5, it will be concluded that if *de facto* control of the oil industry is to be achieved, the government and the international oil companies (IOCs) must vigorously pursue the training and employment of Nigerian personnel. In addition, the government must also encourage the participation of indigenous oil companies in the exploration and development of its oil resources.

The importance of this thesis lies in the fact that oil is the single most important raw material in Nigeria's trade both in volume and in value and contributes over ninety per cent (90%) of Nigeria's foreign exchange earnings. The oil industry could thus provide all the capital needed for Nigerian's economic development.

1.1. The World Oil Industry in Retrospect

The role of oil in the world economy is a major feature of the second half of the 20th century. It is both the most important source of energy and the largest internationally traded commodity.[1] Our civilization depends on oil more than any single commodity.[2] The scale of capital involved in oil development and exploitation, the scope of the trade in oil, the size, sophistication and complexity of the organizations involved and the potential financial rewards make the industry unique.[3]

Between 1930 and 1970, the industry was dominated by seven major international oil companies (IOCs) which were able to remain in control through a sophisticated and well developed vertical integration of their operations.[4] This covered the full range of upstream and downstream activities, extending all the way from exploration and production, through transportation and refining, to the marketing and retailing of products.[5] These "seven sisters", as the major IOCs were widely known are British Petroleum, Exxon, Gulf, Mobil, Royal Dutch/Shell, Standard Oil of California, and Texaco.[6]

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[1] (1984) February OPEC Bulletin at 55 and Z. Mikdashi, *The Community of Oil Exporting Countries* (New York: Cornell University Press, 1972) at 17.

[2] C. Tugendhat & A. Hamilton, *Oil the Big Business* (London: Eyre Methuen, 1975) at 1. The world daily average production of crude oil for 1990 was 61.5 million barrels. See World Oil, August 1991 at 28.

[3] OPEC Bulletin, *supra*, note 1 at 55.

Until the mid - 1960s, the governments of producer countries were only involved in the oil industry to the extent that they received royalties and other payments for crude oil leaving their territories. The ability of the major IOCs to control the world oil market rested on the concession system under which they had virtually entire control over oil exploration and production in some producing countries.[7] In the late 1950s and early 1960s, a number of factors came into existence which had a profound cumulative effect on the shape of the world oil industry. These factors included:[8]

(i) The appearance of European competitors. These companies were established by the governments of some European countries, such as Compagnie Francaise des Petroles (C.F.P.) of France and Ente Nazionale Idrocarburi (E.N.I.) of Italy;

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[4] *Ibid*. See also M.S. Al-Otaiba, *OPEC and the Petroleum Industry* (New York: John Wiley & Sons Inc., 1975) and T. Turner, "Nigeria: Imperialism, Oil Technology and the Comprador State" in P. Nore & T. Turner, *Oil and Class Struggle* (London: Zed Press, 1980) at 199.

[5] OPEC Bulletin, *ibid*.

[6] *Ibid*. See also Mikdashi, *supra*, note 1 at 35.

[7] OPEC Bulletin, *ibid*. at 55-56.

[8] *Ibid*. at 57-58. See also P.R. Odell, *Oil and World Power - A Geographical Interpretation* (New York: Taplinger Publishing Company, 1970) at 11-22.

(ii) the appearance of a number of large oil companies, known as the independents. These companies where mostly based in the United States. The independents began entering into oil exploration and production agreements, offering producer governments significantly more attractive terms than those of the major IOCs;

(iii) the formation of the Organization of Petroleum Exporting Countries (OPEC) in 1960.[9] The formation of OPEC marked the beginning of a radical departure from the dominant position occupied by the major IOCs in the world oil industry. By 1974 OPEC was in a position to take over direct control of oil pricing from the major IOCs and some member countries had gained a controlling influence over their oil industries through active participation in the upstream phases, either through nationalization, or through new forms of participation agreements with the oil companies; and

(iv) the establishment of national oil companies (NOCs) in oil producing states. These companies played a crucial role in developing awareness and experience, especially in the area of production and marketing. It was through the NOCs that producer countries began to gain a greater share of their crude oil production.

---

[9] OPEC was formed in September 1960 as a direct response to the challenge posed by the major international oil companies (IOCs), which arbitrarily and unilaterally reduced the posted price of crude oil in February 1959 and again in August 1960. See I.A. Almutrif, "OPEC, Western Dependency and the Moderate Role of Saudi Arabia" (1988) March OPEC Bulletin 9 at 9.

As a result of these factors, the major IOCs gradually lost control over direct access to crude oil.[10] For several oil producing developing countries, this change was not only significant, but also long overdue since the oil industry is the main source of their foreign exchange earnings.[11] In the next section, we shall briefly examine Nigeria's role in the world oil industry.

1.2. Nigeria's Role in the World Oil Industry

Nigeria benefited immensely from the changes which occurred in the world oil industry between 1960 and 1975.[12] Presently, Nigeria is the largest producer of crude oil in Africa and one of the world's largest exporters.[13] A number of factors have been responsible for the rapid development of Nigeria's oil industry, chief among these being the "discovery of such a wealth of indigenous hydrocarbon resources during a period of soaring world energy demand."[14]

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[10] OPEC Bulletin, *supra*, note 1 at 58.

[11] *Ibid*. See also Mikdashi, *supra*, note 1 at 17.

[12] These benefits are reflected in the changes which occurred in Nigeria's oil industry between 1969 and 1973. These changes are discussed in chapters 2 & 3 respectively.

[13] Nigeria's productive capacity for 1990 was between 1.8-1.9 million barrels of oil per day. See *International Petroleum Encyclopedia* Vol.24 (Tulsa, Oklahoma: Pennwell Publishing Co., 1991) at 133. In the second quarter of 1992 the daily productive capacity rose to 2 million barrels of oil. See (1992) June 1-7 West Africa Magazine at 927.

The importance of Nigeria in the world oil industry explains the presence of the major IOCs in its oil industry. With the exception of Standard Oil of California, all the IOCs are operating in Nigeria. A wide variety of factors influence oil company operations in Nigeria. These include:[15]

(i) The location of Nigerian crude oil. Advantages of location include the security of supply routes to Western Europe, particularly Germany, which is by far the most important market for Nigerian petroleum exports in Europe. With the constant threat of upheaval in the Middle East, Nigerian crude oil is indeed favourably located, though not quite so auspiciously as that of its North African competitors. In addition, Nigeria has relatively good access from a competitive point of view to its secondary markets - North America (United States and Canada) and South America (Argentina, Brazil and Uruguay) - though less so than Venezuela as far as North America is concerned;

(ii) the quality of Nigerian crude oil. Advantages of quality associated with Nigerian crude oil derive in large part from its relatively low sulphur content. This will become increasingly important as legislation concerning air pollution is passed in consuming countries.[16]

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[14] (1985) July/August OPEC Bulletin at 24.

[15] S.R. Pearson, *Petroleum in the Nigerian Economy* (California: Stanford University Press, 1970) at 18-20. See also Odell, *supra*, note 8 at 88-91.

Nigeria, therefore, has an important role to play in the world oil industry.[17] Let us now examine the history of oil in Nigeria.

1.3. The History of Oil in Nigeria.

The search for oil in Nigeria dates back to 1908 [18] when the German firm known as Nigerian Bitumen Company started drilling and exploring for oil within the Okitipupa area, about 200 kilometres east of Lagos. The search was unsuccessful as oil was not found in commercial quantities.[19] The activities of the German firm ceased as a result of the first world war.[20] Interest in the possibility of discovering oil in Nigeria revived in 1937 with the establishment of Shell/D'Arcy Petroleum Development Company of Nigeria, an affiliate of the mineral oil companies Shell Petroleum Company and British Petroleum Company.[21] In November 1938 Shell-BP received an oil exploration license (OEL) covering the whole of Nigeria (357,000 square miles) from the British colonial government.[22]

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[16] Technology is however, available to remove sulphur from crude oil. Libya, Algeria and Indonesia also produce crude oil with a low sulphur content. With the exception of the United States and the former USSR, all major crude oil producers produce crude oil with a high sulphur content. See Pearson, *ibid.* at 19-20.

[17] The most important destination for Nigeria's crude oil exports are the United States, the Netherlands, the United Kingdom, the West Indies, France and Germany, in descending order of magnitude. For example, in 1981, of the total quantity of 1.22 million barrels of crude oil exported daily from Nigeria, the United States bought 33.37%, the Netherlands 11.76%, Dutch Antilles 6.37%, West Germany 5.83%, Italy 4.72%, Curacao 3.30%. Other importers of Nigerian crude oil are Brazil, Ghana, Sweden, Belgium, Ivory Coast, Senegal, Denmark, Sierra Leone and Japan. Source: (1985) July/August OPEC Bulletin at 33. In the third quarter of 1989, Nigeria exported 11.883 million metric tons of crude oil to the United States, 1.370 million metric tons to Germany, 967 thousand metric tons to the Netherlands, 702 thousand metric tons to France, 479 thousand metric tons to Canada, 408 thousand metric tons to Italy and 247 thousand metric tons to the United Kingdom. Source: Quarterly Oil Statistics and Energy Balance (Third Quarter of 1989), published by the Organization for Economic Co-operation and Development (OECD).

[18] The first piece of legislation on petroleum in Nigeria was the *Petroleum Ordinance* of 1889, which was followed by the *Mineral Regulation (Oil) Ordinance* of 1907, both of which laid down a basic framework for the development of petroleum and its natural resources. The 1907 Ordinance stipulated, *inter alia*, that only British subjects or companies controlled by British subjects would be eligible to explore for Nigerian oil resources. In fact this provision is a paradox, as the first company ever to undertake exploration in Nigeria was the German Bitumen Company in 1908. Grants to explore for petroleum may also have been given under the provisions of *Order No. 19* of 1909 Laws of Southern Nigeria. See Y. Omorogbe, "The Legal Framework for the Production of Petroleum in Nigeria" (1987) 5 No.4 J.E.N.R.L. 273 at 273. An examination of Nigerian statutes would however, reveal that the major constituent of the laws which touch upon the exploration and production of petroleum, was the *Mineral Oils Ordinance* of 1914 (Cap.120 of the Laws of the Federation of Nigeria 1958 edition). This Ordinance was promulgated to "regulate the right to search for, win and work mineral oils." See *Basic Oil Laws and Concession Contracts, South and Central Africa (Original Text)* 1959. It appears that the 1914 Ordinance was inspired by the activities of the German firm known as Nigerian Bitumen Company. A new section 10 was added to the 1914 Ordinance by the *Mineral Oils (Amendment) Act* 1950 whereby the submarine areas of Nigeria's territorial waters were brought under the ambit of the 1914 Ordinance. By another amendment in 1959, the legislative competence of Nigeria's Federal legislature was pronounced over the submarine areas of other waters which the legislature may decide to legislate upon in future, in matters relating to mines and minerals. This right is recognised under *Article* 2 of the Geneva Convention on the continental shelf 1958. Section 3(1) of the *Minerals Act* 1946, stipulated that: "The entire property in and control of all mineral oils, on under or upon any lands in Nigeria, and all rivers, streams and watercourses throughout Nigeria, is and shall be vested in the crown...." See G. Etikerentse, *Nigerian Petroleum Law* (London:

After a five year interruption caused by the second World War, Shell-BP intensified its exploration activities during the 1946-1951 period. In 1951 Shell-BP drilled its first wildcat well; it came up dry. During the next four years the company concentrated efforts in the cretaceous areas rimming the Niger Delta in the southern part of Nigeria without discovering any oil producing wells.

Macmillan, 1985) at 2 & 5.

[19] (1982) November OPEC Bulletin at 21. See also Etikerentse, *ibid.* at 1-23.

[20] Etikerentse, *ibid.* at 1.

[21] Pearson, *supra*, note 15 at 15. See also E.O. Egbogah & W.I. Oronsaye, "Nigerian Oil's Future Prospect Seen Keyed to Government Policies" (1979) June 18/25, Vol.X, Supplement Nos. 24/25 OPEC Bulletin at 1 and "OPEC Member Country Profile: Nigeria" in (1979) September 17/24, Vol.X, Supplement Nos. 37/38 OPEC Bulletin at v.

[22] L.H. Schätzl, *Petroleum in Nigeria* (Ibadan: Oxford University Press, 1969) at 1. See also Pearson, *ibid.*

After shifting focus to the tertiary area of the Niger Delta, Shell-BP made Nigeria's first commercial discovery in 1956 at Oloibiri in what is now Rivers State. Towards the end of 1956, another discovery was made at Afam, also in Rivers State.[23] These finds were rapidly developed and by 1958, production had reached 5,100 barrels per day and the first shipment of Nigerian crude oil was made to Europe.[24] Nigeria was, thus, ushered onto the international oil stage.[25]

Geological and geophysical investigations showed that the most favourable oil-yielding structures lay in the Niger Delta, situate in the southern part of Nigeria.[26] By 1957 Shell-BP had voluntarily reduced its acreage to 40,000 square miles of oil prospecting licenses (OPLs). Of this acreage, Shell-BP converted nearly 15,000 square miles into oil mining leases (OMLs) in 1960 and 1962 and returned the remainder of its holdings to the Nigerian government.[27] Unaffected by competitors, Shell-BP was able to select at its leisure until 1962, 15,000 square miles of the 40,000 square miles it held in 1957.[28] The area it chose included the sites that geological and geophysical surveys indicated were most promising for the formation of crude oil deposits.[29] The role played by Shell-BP during this period is succinctly described by Schätzl:[30]

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[23] M. Ajomo, "Law and Changing Policy in Nigeria's Oil Industry" in J.A. Omotola's ed., *Law and Development* (Lagos: University of Lagos Press, 1987), 84 at 86.

[24] *Ibid.*

[25] Pearson, *supra*, note 15 at 15.

[26] Schätzl, *supra*, note 22 at 1.

[27] Pearson, *supra*, note 15 at 15.

[28] Schätzl, *supra*, note 22 at 3.

> The opportunity of exercising an autonomous strategy throughout two decades in the realm of concession politics brought about the result that this company today possesses the optimal concession site in the country. Its monopolistic position in the past with respect to licence selection affords Shell-BP both now and in the future a position of dominance in the development of the Nigerian mineral oil industry.

With the increase in Shell-BP's activities, governmental control and regulations were introduced to ensure compliance by Shell-BP in its operations with safe and good oilfield practice, measured by the standards then known in the industry.[31] Accordingly, a set of Regulations known as the *Mineral Oils (Safety) Regulations* 1952 were issued with an effective date of 31 January 1952. The Regulations were made under the powers conferred on the Governor General by section 9 of the *Mineral Oils Ordinance* of 1914. These Regulations have since been replaced by the *Mineral Oils (Safety) Regulations* 1963, which became effective from 11 April 1962.[32]

After Shell-BP's first commercial discovery in 1956, it became necessary to transport the crude oil through long distances between the wellhead and the point of exportation.[33] The *Oil Pipelines Act* of 1956 was passed with provisions designed to meet the requirements of this development in Shell-BP's operations. Amendments to certain provisions of this Act were effected by the *Oil Pipelines Act* of 1965. Also, in order to specifically tax the realised profits of oil companies, separately from those of other companies engaged in other enterprises, the *Petroleum Profit Tax Act* was promulgated in 1959 with retroactive effect from 1 January 1958.[34]

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[29] *Ibid.*

[30] *Ibid.* Today, Shell is the largest operator in Nigeria, with a production capacity of 1 million barrels of oil per day. See World Oil, August 1991 at 91.

[31] Etikerentse, *supra*, note 18 at 2.

[32] *Ibid.*

1.3.a. The Appearance of Competitors

With the repeal in 1958 [35] of section 6(1)(a) of the *Mineral Oils Ordinance* of 1914, which disqualified non-British companies from receiving exploration licences, the monopoly of exploration rights given to Shell-BP in 1938 was gradually broken.[36] Some IOCs soon appeared in Nigeria, taking up oil prospecting licences (OPLs) on concessions voluntarily relinquished by Shell-BP.[37] This development was in line with the government's policy of increasing the pace of exploration while at the same time ensuring that the country was not overdependent on one company.[38] Thus, after Nigeria's independence in

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[33] *Ibid.* at 2-3.

[34] *Ibid.* at 3.

[35] By Section 2 of the *Mineral Oils (Amendment) Act 1958.*

[36] Ajomo, *supra*, note 23 at 86.

[37] Etikerentse, *supra*, note 18 at 2.

[38] See Annual Report of the Mines Division, Ministry of Mines and Power, 1958/1959, referred to in Ajomo, *supra*, note 23 at 86 n.7. According to Ajomo at 86, the government's policy must have been the result of the attainment of some measure of internal self-government in 1959, which carried with it, the

1960, the Nigerian Gulf Oil Company which was a subsidiary of Gulf Oil Corporation of America, was licensed to explore for petroleum in 1961.[39]

Other IOCs that were represented in Nigeria and which secured exploration licences about the same time, included Mobil Oil, Texaco, Sunray-Tenneco, Occidental, Agip the Italian state-owned oil company as well as its French counterpart of Safrap, which later became Elf.[40] The appearance of these IOCs, opened up a new phase of development in the oil industry and in 1964, Gulf Oil Company made the first off-shore discovery of oil in Delta State, in the southern part of Nigeria.[41] According to Ajomo:[42]

> The open door policy which began in 1959 engendered a spirit of healthy rivalry from which the industry benefited tremendously.

The principal legislation under which oil rights were granted to the IOCs was the *Mineral Oils Ordinance* of 1914. We will now examine the various types of oil rights which could be acquired by an oil company wishing to undertake oil exploration and production in Nigeria before 1969.

1.3.b. The Acquisition of Oil Rights before 1969

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right to formulate independent internal policies.

[39] Etikerentse, *supra*, note 18 at 3. According to Schätzl, the first company which took part in the search for crude oil in Nigeria after Shell-BP, was Mobil Exploration Nigeria Ltd., an affiliate of the American Socony-Mobil Oil Company. In 1955 this company obtained an exploration licence encompassing 281,782 square miles for all of the abandoned Shell-BP territory in the Northern part of Nigeria. It was on December 1, 1961 that Gulf Oil Company obtained oil prospecting licences from the Nigerian government. See Schätzl, *supra*, note 22 at 3-4.

[40] Etikerentse, *ibid*.

[41] Ajomo, *supra*, note 23 at 86.

[42] *Ibid*. at 86-87.

In order to start exploration, development, or production activity in Nigeria, the IOCs needed the authorization of the government of the federation of Nigeria.[43] Thus, section 3 of the *Mineral Oils Ordinance* of 1914 provided:[44]

> It shall not be lawful for any person to search or drill for or work mineral oils within or under any lands in Nigeria except under a licence or lease granted by the Minister under this Ordinance. Provided that nothing in this Ordinance contained shall affect any licence or lease granted under any Ordinance repealed by this Ordinance, which licence or lease shall for all purposes have effect as if this Ordinance had not been made.

Initially the Federal Minister of Mines and Power on behalf of the government negotiated the concessionary agreements with the interested oil companies individually.[45] Since 1959, as a result of a government Notice, the acquisition of oil rights by the IOCs became standardized.[46] This Notice distinguished between exploration, prospecting and mining rights according to the stage of development in the concession areas. Let us examine the main provisions of this Notice.

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[43] Schätzl, *supra*, note 22 at 77.

[44] See Cap. 120 of the Laws of the Federation of Nigeria 1958 edition reproduced in *Basic Oil Laws and Concession Contracts, South and Central Africa (Original Text), Supplement* Nos.31-35.

[45] Under Sections 4 & 5 of the *Mineral Oils Ordinance 1914*, the Minister of Mines and Power was authorised to grant licences or leases on such terms and conditions as he may deem fit, subject to the provision relating to payment of compensation for disturbance of surface rights.

[46] See Government Notice No.2675 published in the *Federation of Nigeria Official Gazette* No. 76 of the 17th of December, 1959 as amended by Notice No. 576 published in the *Federation of Nigeria Official Gazette* No. 16 of 31st March, 1960. These Gazettes are reproduced in *Basic Oil Laws and Concession Contracts, South and Central Africa (Original Text), Supplement* Nos. 1-5. [Hereinafter Notice No. 2675]. These Notices were issued pursuant to the powers conferred on the Governor General under section 9 of the *Mineral Oils Ordinance of 1914*. According to Olisa, the contents of these notices and forms do not exhaust the discretion given to the Minister under sections 4 & 5 of the Ordinance. See M.M. Olisa, *A Comparative Study of the Acquisition of Oil and Gas Rights in Africa* (Edmonton, Alberta: University of Alberta, LL.M Thesis 1967, Unpublished) at 57-58.

1.3.b.i. Oil Exploration Licence (OEL) [47]

The main feature of an OEL was that the oil companies had the right to carry out geological and geophysical exploration for oil over the land and territorial waters of Nigeria excluding land approved for grant or already granted to oil operators. An OEL did not include the right to drill for petroleum in the concessionary area.[48]

Exploration rights could be granted to several companies within the same concession area and could be granted for any area up to 10,000 square miles.[49] In addition, the government was under no obligation to convert expired exploration licences into prospecting or mining rights.[50] An OEL was valid for a period of one year, with a possible extension for another year and could be converted into a prospecting licence in respect of any area found to be promising in petroleum deposits.[51] The fee for each calendar year was fifty pounds.

1.3.b.ii. Oil Prospecting Licence (OPL) [52]

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[47] See Generally, Notice No. 2675, *ibid.* and also Schätzl, *supra*, note 22 at 77-78.

[48] Notice No. 2675, *ibid.* See also Schätzl, *ibid.* at 78.

[49] Notice No.2675, *ibid.* and Schätzl, *ibid.*

[50] Notice No. 2675, *ibid.* and Schätzl, *ibid.*

[51] Notice No. 2675, *ibid.* and Schätzl, *ibid.*

[52] See Generally, Notice No. 2675, *ibid.* and Schätzl, *ibid.* See also Model OPL for land and continental shelf in *Basic Oil Laws and Concession Contracts, supra*, note 46.

An OPL could either be in respect of the mainland including a three-mile coastal limit and/or for the continental shelf areas; and the location also affected the duration of the OPL.[53] While licences for mainland areas were valid for three years and could be further extended for another period of two years, the licences for continental shelf areas were granted for four years with a possibility for further extension for another three years. Unlike the exploration licence, a prospecting licence granted to the oil companies the exclusive right to carry out geological and geophysical investigations in their concession areas, to drill, export and to refine the petroleum in Nigeria.

Several obligations were imposed on the holder of a prospecting licence. There was the obligation to start geophysical investigation within six months and to drill at least 12,000 feet of wells on the mainland within three years, and four years in the continental shelf. There was also the obligation to train Nigerians in the art of drilling and production of petroleum. The extent of the obligation was however, not defined. The maximum area of an OPL was 2,000 square miles on land and 1,000 square miles on the continental shelf.

In addition, there were financial obligations imposed on the holder of an OPL. The rent for an OPL was two shillings (2s) per square mile per annum. A premium of five hundred thousand (500,000) pounds for 1,000 square miles was payable for the continental shelf. For land areas, the premium was to be determined by the government. Royalties were also imposed on all crude oil, natural gas and casinghead spirit won, saved or recovered at the following rates:[54]

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[53] Notice No. 2675, *ibid*.

(i) Four shillings (4s) per ton on all crude oil of a potential production of up to 500,000 tons per annum, thereafter;

(ii) 12 1/2% of the wellhead value of all crude oil won on land areas including the off-shore area within the three mile limit seawards;

(iii) 10% of the wellhead value of all crude oil won on the continental shelf between the three mile limit and the 10 fathom depth line;

(iv) 8% of the wellhead value of all crude oil won on the continental shelf beyond the 10 fathom depth line;

(v) 10% of the wellhead value on all casinghead spirit; and

(vi) Two pence (2d) per 1,000 cubic feet of natural gas.

When an OPL expired, there was a requirement that it must either be handed back to the government or converted into a mining lease.

1.3.b.iii. Oil Mining Lease (OML) [55]

OMLs were for terms of thirty years with the right to renewal for a further thirty years on land and forty years with the right to renewal for a further forty years on the continental shelf. Lessees had the exclusive right to take every measure necessary to exploit and to develop a petroleum industry in their concession areas. Like the oil prospecting licensee, the lessee of an OML was under an obligation to train Nigerians in the art of drilling and production of petroleum during the whole term of the mining concession. The area of an OML may be of any size approved by the government.

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[54] *Ibid.*

[55] *Ibid.* See also Schätzl, *supra*, note 22 at 80 and Model OML for the continental shelf in *Basic Oil Laws and Concession Contracts*, *supra*, note 46.

In addition, the lessee of an OML was required to operate with the aid of experts, up-to-date equipment, machinery and methods. Financial obligations were also imposed on the lessee of an OML. The rent for an OML was two shillings and six pence (2s 6d) per acre for the first year increasing to ten shillings (10s) per acre in the sixth and subsequent years. The premium payable by the lessee of an OML was calculated on the same basis as that payable by the licensee of an OPL. Royalties were also imposed on all crude oil, natural gas and casinghead spirit won, saved or recovered at the following rates: [56]

(i) 12 1/2% on the wellhead value of all crude oil won on land areas including the offshore area within the three mile limit seawards;

(ii) 10% of the wellhead value of all crude oil won on the continental shelf between the three mile limit and the 10 fathom depth line;

(iii) 8% of the wellhead value of all crude oil won on the continental shelf beyond the 10 fathom depth line;

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[56] Notice No. 2675, *ibid.*

(iv) 10% of the wellhead value of casinghead spirit; and

(v) Two pence (2d) per 1,000 cubic feet of natural gas.

According to Schätzl:[57]

> The laws were meant to induce the oil companies, by favourable contractual terms, to start exploring for petroleum in the Niger Delta's dense forests and mangrove swamps despite the high expenditures necessary for exploring and developing in that area.

The government's economic policy was reflected in the small financial benefits it received from the oil companies. This meant that the terms of these concessions were more favourable to the oil companies.[58] For example, in addition to the rents, royalties and premiums payable to the government, which have been referred to above, the following provisions were also favourable to the oil companies:[59]

(i) Royalties and other duties due to the government were included in the 50% share of profits due to the government.[60]

(ii) Profits were assessed on the basis of realised proceeds.[61]

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[57] *Supra*, note 22 at 94.

[58] *Ibid*. See also Ajomo, *supra*, note 23 at 87.

[59] Schätzl, *ibid*.

[60] Under the *Petroleum Profit Tax Act* of 1959, the Nigerian government instituted the standard 50/50 arrangement for the sharing of profits with the IOCs.

[61] This meant that the oil companies applied its realised price to the volume of crude oil produced and exported to calculate gross proceeds. This valuation of output served as the basis for calculating royalties and taxes on profits. In 1967, the Nigerian government set a posted price for crude oil. See Pearson, *supra*, note 15 at 23-25. A posted price is a price fixed by government order on the basis of which royalties and taxes are assessed. See H.R. Williams & C.J. Meyers, *Manual of Oil and Gas Terms* (New York: Matthew Bender & Co., 1984) at 656.

(iv) The depreciation rates conceded to the oil companies were higher than justified by economic principles.[62]

The OELs, OPLs and the OMLs granted under the *Mineral Oils Ordinance* of 1914 were the concessionary rights under which oil companies could operate in Nigeria before equity participation and contractual joint venture requirements were imposed in 1969 and 1973 respectively.[63]

1.3.c. Subsequent Developments

Between 1960 and 1971, the economic dominance by the IOCs over Nigeria's oil resources and other oil producing countries in the developing world continued.[64] A similar situation prevailed in countries that were producers of other natural resources.[65] Attempts by these countries to amend existing legislation relating to their natural resources in their favour usually lead to tough negotiations.[66] Against this background a large number of natural resources producing countries approached the renegotiation or restructuring of these concession contracts as a legitimate part of the decolonization process, arguing that their sovereignty over natural resources would be jeopardized if these agreements were to last.[67] In Nigeria, the important petroleum discoveries and the increase in petroleum production led to a change in the federal government's economic policy towards the IOCs.[68] At this particular period, the federal government had no equity interest in any of the IOCs. Complicated negotiations took place between the federal government and the IOCs concerning the extent of modifications.[69]

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[62] Schätzl, *supra*, note 22 at 88, where the author submits that: "The method of depreciation practised in Nigeria charges the various accounting periods with decreasing depreciation expenditure; the initial years are much more heavily charged than the later ones.In a geometrically declining rate of depreciation a complete write-off of an installation is never accomplished but the oil companies can write-off the balance all at once, whenever the equipment cannot be used any more for petroleum exploration."

[63] Equity participation and contractual joint ventures will be discussed in chapters 2 & 3 respectively.

[64] S.K.B. Asante & A. Stockmayer, "Evolution of Development Contracts: The Issue of Effective Control" in *Legal and Institutional Arrangements in Mineral Development*, (London: Mining Journal Books, 1982), 53 at 53.

[65] *Ibid.*

[66] Schätzl, *supra*, note 22 at 94.

However, unlike in other oil producing developing countries, the situation in Nigeria was made easier by existing financial arrangements between the government and the IOCs.[70] These financial arrangements were contained in the covenants that each company had signed with the government. These covenants were not contained in the OMLs, but were in separate documents and though they reportedly differ somewhat in detail, the major financial arrangements apply uniformly to all the IOCs.[71] In each company's covenant with the Nigerian government there was a provision usually termed the most-favoured-nation clause.[72] In this provision the oil companies operating in

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[67] R. Kemper, "The Concept of Permanent Sovereignty and its Impact on Mineral Contracts in *Legal and Institutional Arrangements in Mineral Development*, *supra*, note 64 at 32.

[68] Schätzl, *supra*, note 22 at 94.

[69] *Ibid.*

[70] See Shell-BP's financial arrangement with the government, Port Harcourt, 1965 referred to in Schätzl, *ibid.* at 95 n.38

[71] Pearson, *supra*, note 15 at 22.

[72] *Ibid.* at 24.

Nigeria promised that they would negotiate with and, by implication, give terms to the Nigerian government equal to the most favourable terms accorded to any other government on the continent of Africa or in the Middle East.[73]

In addition, separate agreements were entered into between the Nigerian government and some IOCs in which conditions relating to:[74]

> (i) the percentage of the companies profits that would be subject to taxation under the *Petroleum Profit Tax Act* of 1959;
>
> (ii) variation in the royalty amounts due and payable at a given period;
>
> (iii) revision (usually upward) in the posted price to be applied to crude oil for the purposes of taxation; and
>
> (iv) the levy on ships exporting crude oil from Nigerian terminals.

Although these financial arrangements and agreements had the effect of amending existing provisions of some legislation, it must be stressed, however, that steps were usually taken by the government to formally reduce the terms of these financial arrangements and agreements into law.[75] In order to give further legal backing to any action taken under these financial arrangements and agreements, prior to legislation, retroactive commencement dates were frequently provided for.[76] For example:[77]

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[73] *Ibid.* at 24-25. In 1967, the *Petroleum Profits Tax (Amendment) Decree* was promulgated. This Decree amended the Nigerian *Petroleum Profits Tax Act* 1959 to Libya's Petroleum Legislation in accordance with the covenants between the government and the IOCs. For example, under the 1967 Decree, the basis of tax calculations was no longer "realised prices", but "posted prices." See Schätzl, *supra*, note 22 at 96-98.

[74] Etikerentse, *supra*, note 18 at 3.

[75] *Ibid.*

(i) The *Oil Terminal Dues Act* 1969, brought into law the terms of some of the long standing agreements; hence the stipulation of 1 January 1965 as the commencement date; and

(ii) the *Petroleum (Drilling and Production) (Amendment) Regulations* 1979, which introduced new royalty rates, was effective on 1 April 1977, although its terms had been implemented long prior to its promulgation.

1.3.c.i. The Influence of the United Nations

On the international scene, the conflict between natural resources producers, mostly from the developing countries, and the multinational companies from the developed countries led to the United Nations resolution on permanent sovereignty over natural resources, [78] which shifted the balance of power from the IOCs to the developing countries.[79] This resolution rejected the idea of investor ownership and control of a state's natural resources.[80] No doubt, Nigeria benefited from this resolution and this was reflected in the changes in its laws and contractual agreements with the IOCs.[81]

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[76] *Ibid.*

[77] *Ibid.* at 3-4.

[78] G.A. Res. 1803, 17 U.N. GAOR, Supp. (No.17) 15, U.N.Doc.A/5217 (1962). For a detailed discussion of the origin and legal status of the principle of permanent sovereignty over natural resources, see chapter 4.

[79] A.S. El-Kosheri & T.F. Riad, "The Law Governing a New Generation of Petroleum Agreements: Changes in the Arbitration Process" (1986) 1 ICSID Rev. 257 at 257.

[80] Asante & Stockmayer, *supra*, note 64 at 53.

It appears that the principal objective of the Nigerian government in granting oil rights to the IOCs for oil exploration and production prior to 1969, was:[82]

> To secure an investment of risk capital and the technical and managerial skills of an IOC to carry out as thorough and as rapid an exploration of its prospective areas as is reasonably possible.

The IOCs' principle objective of maximisation of its long-run earnings from its overall global operations determined its global exploration strategy.[83] It was, therefore, inevitable that a conflict would arise when the Nigerian government changed its policy goal from regarding the oil industry as only a revenue-yielding venture to other interrelated goals which expressed certain values such as: "Speeding the achievement of financial self reliance, acquiring technology and expertise and the overall ownership and control of its natural resources."[84]

1.3.c.ii. The Influence of the Organization of Petroleum Exporting Countries (OPEC)

Similarly as a result of the influence of the Organization of Petroleum

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[81] See the *Petroleum Act* of 1969 and the various contractual agreements between the NNPC and the IOCs which are dealt with in chapters 2 & 3 respectively.

[82] K. Hossain, *Law and Policy in Petroleum Development* (London: Frances Pinter (Publishers) Ltd., 1979) at 43.

[83] *Ibid.*

[84] K.W. Blinn, et al *International Petroleum Exploration and Exploitation Agreements - Legal, Economic, and Policy Aspects* (New York: Barrows Co., Inc., 1986) at 49.

Exporting Countries (OPEC),[85] the Nigerian National Oil Corporation (NNOC) was formed in 1971[86] and in July of the same year, Nigeria joined OPEC. It appears that the formation of NNOC was in response to OPEC resolutions and policy statements which required the existence of a state oil corporation as a condition precedent for state participation in the oil industry.[87]

In 1977, the NNOC was merged with the Oil Ministry to form the Nigerian National Petroleum Corporation (NNPC).[88] The NNPC is an agency of the federal government and exercises supervisory and regulatory control over the IOCs operating in Nigeria.[89] In 1972, all rights to explore for and produce mineral oils in Nigerian territory were reserved by the federal government for the NNPC with the exception of those areas in which there were subsisting grants of petroleum rights.[90] The areas reserved included areas subsequently surrendered, relinquished or forfeited to the government.[91]

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[85] OPEC Resolution XV1.90 "Declaratory Statement of Petroleum Policy in Member Countries" 24-25 June 1968. See *OPEC Official Resolutions and Press Releases* 1960-1990 at 62. This resolution called on all member countries to acquire participation in the exploration of their natural resources.

[86] *Decree No. 18 of 1971.*

[87] OPEC Resolution XV1.90, *supra*, note 85. On OPEC see Al-Otaiba, *supra*, note 4 and P. Terzian, *OPEC: The Inside Story* (London: Zed Books, 1985).

[88] *Decree No. 33* of 1977. For the growth of the NNPC, see Etikerentse, *supra*, note 18 at 16, M.M. Olisa, *Nigerian Petroleum Law and Practice* (Ibadan: Fountain Books, 1987) at 181 and M.M. Olisa, "National Oil Companies - Quo Vadis? The Nigerian National Petroleum Corporation" (1981) 1 Energy Law 87 at 91-99.

[89] This function is carried out by the Department of Petroleum Resources. Under *Decree No. 33* of 1977, it was originally known as the Petroleum Inspectorate. As a result of the reorganization which took place in March 1988 it acquired the new name Department of Petroleum Resources.

[90] Government Notice No. 311 of 24 February 1972 referred to in Etikerentse, *supra*, note 18 at 17 n.63.

1.3.d. An Assessment

In this chapter, we have examined the changes which took place in the world oil industry between 1960 and 1970 and how these changes led to a shift in the balance of power from the IOCs to oil producing developing countries. This examination has been necessary because these changes also affected developments in Nigeria's oil industry. We have also briefly examined Nigeria's role in the world oil industry. Our main focus was, however, on the growth and development of Nigeria's oil industry from its meagre beginning in 1908, and the subsequent developments which took place in the industry. These subsequent developments, together with the increase in the number of active oil companies and the experience gained by Nigeria from the conditions that existed in OPEC countries, meant that the frail structures of the *Mineral Oils Ordinance* of 1914, under which oil rights were acquired by the IOCs prior to 1969, could no longer sustain the modern pressure and trends in the industry. The *Petroleum Act* of 1969 was, thus, promulgated. This Act which repealed the *Mineral Oils Ordinance* of 1914 and its amendments, comprised the first major attempt at producing a detailed and comprehensive law for the grant and acquisition of rights to search for and win oil in Nigeria.

Today the importance of oil to Nigeria's economy cannot be overemphasised, since over ninety per cent (90%) of Nigeria's foreign exchange earnings are derived from the oil industry.[92] It was, however, not until 1971 that Nigeria's oil industry witnessed fundamental changes in the modes of acquisition of oil rights with the introduction of equity participation and contractual joint ventures. These changes reflected the fundamental shift in the bargaining power between the Nigerian government and the IOCs.[93]

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[91] An oil exploration licensee may terminate or effect partial surrender of the licence on the payment of a fee of one hundred naira (N100). An oil prospecting licensee or oil mining lessee may terminate or surrender by giving the minister three months notice to that effect. See G. Utomi, "Special Report on Nigeria," (1991) April Special Supplement I.F.L. Rev. 58 at 58.

These agreements must no longer be viewed simply as revenue generating ventures, but as economic development agreements.[94] Economic development agreements are of vital importance to the development of Nigeria. They provide an avenue for the acquisition of petroleum technology, the training of Nigerians and, thus, contribute to the increase in Nigeria's growth rate. Although these changes in the oil industry led to the demise of the traditional concession, it is debatable whether in terms of *de facto* control of the oil industry there has been any fundamental change. Suffice it to say however, that there was a marked increase in the government's revenue from the oil industry between 1958 and 1980 as a result of the introduction of new modes for the acquisition of oil rights.[95] In chapter 2, we examine the changes introduced by the *Petroleum Act* of 1969.

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[92] (1992) January 6, Oil and Gas Journal at 88.

[93] El-Kosheri & Riad, *supra*, note 79 at 257.

[94] Economic development agreements have been defined as: "Agreements whereby a state engages the capital and technology of a foreign enterprise, typically of one or more developed countries, in an undertaking designed to have a decisive positive impact on the state's overall economic development." See G.A. Bermann, "Contract Between States and Foreign Nationals: A Reassessment" in Hans Smith et al eds., *International Contracts* (New York: Matthew Binder, 1981), 183 at 190.

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[95] In 1958 the government's revenue from crude oil was 3.8 million naira. This rose to 13.12 billion naira at the peak of the 1980 production. See Ajomo, *supra*, note 23 at 87.

Chapter 2

ACQUISITION OF OIL RIGHTS UNDER THE PETROLEUM ACT OF 1969

2.0. Introduction

The main subject of this chapter is the acquisition of oil rights under the *Petroleum Act* of 1969. [1] It does not provide an examination of the entire Act, but rather an analysis of the different modes of acquisition of oil rights and equity participation under the Act. In order to give something more than a descriptive account of the different modes of acquisition of oil rights, some method of assessment needs to be adopted. Here, the different modes of acquisition of oil rights are assessed according to how far they secure the objectives of the government of encouraging exploration and development of its territory so as to have a full assessment of the country's potential.

In the first section, we examine the background to the promulgation of the Act, while in section two, the different modes of acquisition of oil rights under the Act are examined. Finally in section three, we examine equity participation which was the major innovation introduced by the Act.

2.1. The Background to the Act

In 1969, petroleum legislation in Nigeria took a great leap forward, with the promulgation of the Act and its accompanying Regulations.[2] They constituted the first major attempts at producing a detailed and comprehensive law that clearly defined the rights and obligations of a licensee and lessee under one law.[3] They set out the rules for the conduct of petroleum exploration and production "in a more progressive manner."[4]

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[1] [Hereinafter Act].

[2] M. Ajomo, "Law and Changing Policy in Nigeria's Oil Industry" in J.A. Omotola ed., *Law and Development* (Lagos: University of Lagos Press, 1987), 84 at 90.

The promulgation of the Act must be viewed in connection with the situation existing prior to its enactment. Between 1957 and 1960 there emerged persistent calls on the government to nationalize the economy by taking over all foreign interests.[5] Some of the hostility towards foreign investors were expressed during the Nigerian House of Representatives debates on the Shell-BP operations in 1957.[6] A member of the House complained that:[7]

> Nearly all our leading industries are in the hands of foreigners....our cement company, our air transport, our shipping, our tin and other mining industries; now oil and probably iron and steel.

However, these calls were not heeded by the government.[8] The government was aware of the impact of nationalization on the flow of foreign capital investment to a developing country.[9]

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[3] G. Etikerentse, *Nigerian Petroleum Law* (London: Macmillan, 1985) at 4 and also Ajomo, *ibid.*

[4] Ajomo, *ibid.*

[5] Chief O. Awolowo, Presidential Address, Conference of the Action Group, Ibadan, October 12, 1957 referred to in O.A. Osunbor, "Nigeria's Investment Laws and the States Control of Multinationals" (1988) No.1 ICSID Rev.38 at 43.

[6] Osunbor, *ibid.*

[7] J. Wachukwu, House of Representatives Debate 578 (February 1959) referred to in Osunbor, *ibid.* See also, Chief O. Awolowo's address to the Nigerian House of Representatives in 1961 in which he said: "That this House approves in principle the nationalization of basic industries and commercial undertakings of vital importance to the economy of Nigeria", referred to in P.O. Proehl, *Foreign Enterprise in Nigeria - Law and Policies* (North Carolina: University of North Carolina Press, 1965) at 163.

[8] Osunbor, *ibid.* at 44. See Sir Abubakar Tafawa Balewa's (Prime Minister 1960-1966) address to the Nigerian House of Representatives in 1964, in which he said: "It must be obvious that no Nigerian can be content so long as any major sector of the economy is controlled by foreigners. But we are realists and we

The emergence of military rule in 1966 saw a new wave of economic nationalism and renewed calls for the ownership, control and management of the economy by Nigerians.[10] Government under the military, unlike the politicians of the first republic (1960-66), was more responsive to such pressures.[11] It was this change of policy that led to the promulgation of several statutes between 1968 and 1972, including the Act in 1969.[12] The period 1968-72 was commonly referred to as the "indigenization period."[13]

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say so long as there is dearth of Nigerian capital, so long must there be an opportunity for foreign capital in Nigeria. We do not seek the withdrawal of foreign capital from any area of the economy before Nigerian enterprise is able to replace it. When the time for withdrawal has come, due notice will be given." Referred to in Proehl, *ibid.* at 159.

[9] Osunbor, *ibid.*

[10] *Ibid.*

[11] Etikerentse, *supra*, note 3 at 12.

[12] Some of these statutes include, *Banking Act* of 1968, now repealed by the *Banks and other Financial Institutions Decree* of 1991, *Companies Act* of 1968, now repealed by the *Companies and Allied Matters Decree* of 1990 and the *Nigerian Enterprises Promotion Decree* of 1972.

[13] The *Nigerian Enterprises Promotion Decree* 1972 popularly known as the indigenisation Decree. It provided in essence that certain scheduled enterprises were to be reserved exclusively for Nigerian citizens. This Decree was repealed by the *Nigerian Enterprises Promotion Decree* 1977. The 1977 Decree has also been repealed by the *Nigerian Enterprises Promotion Decree* 1989. For a detailed discussion of the background and substantive issues of the indigenization Decrees of 1972 and 1977, see E.I. Kachikwu, *Nigerian Foreign Investment Law and Policy* (Lagos: Mikzek Law Publications Ltd., 1988) at 143-237. See also D. Ijalaye, "Indigenization Measures and Multinational Corporations in Africa" (1981) 26 *Recueil des Cours* 171 and B. Blankenheimer, "Foreign Investment Climate in Nigeria" (1977) 10 Vand.J.Transnat'l L. 589, where the writer uses the phrase "Nigerianization."

Seven years prior to the promulgation of the Act, the United Nations had debated and adopted resolution 1803,[14] which affirmed "the principle of permanent sovereignty over natural resources."[15] It is submitted, that resolution 1803 played an important role in the promulgation of the Act in 1969. This view is supported by section 1(1) of the Act. It provides:

> The entire ownership and control of all petroleum in, under or upon any lands to which this section applies shall be vested in the state....

Similarly, resolution 1803 provides:

> The right of peoples and nations to permanent sovereignty over their natural resources must be exercised in the interest of their national development and the well being of the people of the state concerned....

Although, the Act uses the words "Ownership and Control", resolution 1803 does not. Instead it emphasises "the right of peoples and nations to permanent sovereignty over their natural resources." Since "Ownership and Control" are synonymous with the power of a sovereign state, the Act theoretically affirms the "principle of permanent sovereignty over natural resources." This principle is now generally accepted as a basic principle of international law.[16] It is however, doubtful whether the modes of acquisition of oil rights under the Act are compatible with the principle of permanent sovereignty over natural resources, since *de facto* control of the oil industry is still in the hands of the international oil companies (IOCs).

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[14] General Assembly resolution 1803 (XVII) of 14 December 1962 popularly known as the landmark resolution. This resolution has been developed and reaffirmed in resolution 3021 (S-VI) of May 1, 1974 (Declaration of the Establishment of a New International Economic Order) and *Article* 2 of the Charter of Economic Rights and Duties of States, resolution 3281 (XX1X) of 12 December 1974.

[15] For further discussion of this principle, see chapter 4. The promulgation of the Act was also influenced by OPEC's resolution XVI.90 of 24-25 June 1968, although Nigeria had not joined OPEC at this time, the Act embodied the principles contained in the resolution. This Resolution reaffirmed "the inalienable right of all countries to exercise permanent sovereignty over their natural resources in the interest of their national development as a universally recognized principle of public law." See *OPEC Resolutions and Press Releases* 1960-1990 at 61.

The provisions of section 1(1) of the Act, must now be seen in the light of section 40(3) of the *Federal Constitution of Nigeria* 1979, which provides:[17]

> Notwithstanding the foregoing provisions of this section, the entire property in and control of all minerals, mineral oils and natural gas in, under or upon any land in Nigeria....shall vest in the government of the federation....

This Section merely restated the existing law as contained in the Act and did not have any impact on the existing relationship between the Nigerian government and the IOCs. The federal constitution and the Act, thus, established the federal government's ownership of all petroleum *in situ* within its area of legislative competence.[18] In the next section, we examine the different types of grants that can be acquired from the government in furtherance of the government's rights and powers. Also examined in this section are the nature and content of these grants.

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[16] S.R. Chowdhury, "Permanent Sovereignty Over Natural Resources" in K. Hossain & S.R. Chowdhury eds., *Permanent Sovereignty over Natural Resources in International Law - Principle and Practice* (New York: St. Martin's Press, 1984), 1 at 38. See also, M. Mughraby, *Permanent Sovereignty Over Oil Resources* (Beirut: Middle East Publishing Centre, 1966) at 16.

[17] A similar provision is now contained in the *Federal Constitution of Nigeria* 1989. This constitution is not yet in force.

[18] In some Provinces in Canada, private ownership of oil and gas *in situ* still exists. This is however, an exception rather than the rule. Some other Provinces have vested oil and gas in the Crown. For example, in the Province of Alberta, private ownership of oil and gas *in situ* constitutes ten per cent (10%) of the mineral rights holdings, while in New Brunswick, all oil and natural gas are vested in the Crown. See J.B. Ballem, *The Oil and Gas Lease in Canada* (Toronto: University of Toronto Press, 1985) at 8-11.

2.2. Acquisition of Oil Rights under the Act

The Act provides for the Minister of Petroleum Resources to grant licences for the exploration and prospecting for petroleum as well as the issuing of leases for the mining of petroleum.[19] Any person who wishes to undertake any activity for the exploration or production of mineral oils requires a formal written authorization of the Minister of Petroleum Resources. The oil rights which may be granted by the Minister of Petroleum Resources are:[20]

2.2.a. Oil Exploration Licence (OEL)

An OEL may be granted by the Minister of Petroleum Resources under the powers conferred on him by section 2(1)(a) of the Act. An IOC seeking a grant of an OEL must file with the Minister a completed form 'A' together with the payment of an application fee of one hundred naira (N100). The size of the area applied for must be compact and may not exceed 12,950 square kilometres. The area is required to be bounded by straight lines running in north, south, east and west directions. Exploration licences shall not be granted in respect of areas over which there are existing oil rights, such as oil prospecting licences or oil mining leases granted under the repealed *Mineral Oils Ordinance* of 1914 or the Act. It does not confer on the licensee any exclusive right over the area covered by the licence, and the grant of an OEL shall not preclude the grant of another OEL or an oil prospecting licence or oil mining lease over the same area or any part thereof. The grant of an OEL confers on the licensee the right to carry out aerial and surface geological and geophysical surveys, excluding drilling below 91.44 metres.

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[19] Section 2(1) of the Act. For a detailed examination of the oil exploration licence, oil prospecting licence and oil mining lease, see Etikerentse, *supra*, note 3 at 24-35. The Act retained the framework of the previous law under which pre-1969 grants were made. See *Mineral Oils Ordinance* of 1914 (Cap. 120 of the Laws of the Federation of Nigeria 1958 edition) which was discussed in section 1.3.b. of chapter 1.

[20] See Schedule 1 of the Act and Etikerentse, *ibid*. Contrast with the *Canada Petroleum Resources Act, R.S.C.* 1985, C.36 (2nd Supp.), S.130. [Hereinafter CPRA]. Under the CPRA, petroleum rights may take one of three forms: an exploration licence, a significant discovery licence, or a production licence. These rights can be acquired by "public bids."

An OEL shall terminate on 31 December next following the date on which it was granted, but the licensee shall have the option to renew the licence for one further year if:

(i) It has fulfilled in respect of the licence all obligations imposed by the Act or otherwise;

(ii) the Minister is satisfied with the work done and the reports submitted by the licensee in pursuance of the licence; and

(iii) an application for renewal has been made at least three months before the date of expiry of the licence.

The grant of an OEL shall not confer any right to the grant of an oil prospecting licence or oil mining lease.

2.2.b. Oil Prospecting Licence (OPL)

Under section 2(1)(b) of the Act, the Minister may grant to an applicant an OPL. The procedure for applying for an OPL is the same as that for an OEL. An application for this licence is made to the Minister of Petroleum Resources by the completion of form 'A' with an application fee of two hundred naira (N200). The area applied for is required to have boundaries of straight lines running in north to south and east to west directions. In addition, the area covered by an OPL should be compact, and must not exceed 2,590 square kilometres. An OPL grants to the licensee the exclusive right to explore and prospect for petroleum within the area of the grant. The duration of an OPL shall be determined by the Minister, but shall not exceed five years including periods of renewals. The holder of an OPL may carry away and dispose of petroleum won during prospecting operations, subject to the fulfilment of the obligations imposed by or under the Act.

2.2.c. Oil Mining Lease (OML)

An OML may be granted by the Minister of Petroleum Resources by virtue of his power derived from section 2(1)(c) of the Act. As with the applications for OELs and OPLs, the applicant for an OML files with the Minister of Petroleum Resources a duly completed form 'A' and pays a fee of four hundred naira (N400). The area covered by an OML must be compact and must not exceed 1,295 square kilometres. An OML may be granted only to the holder of an OPL who has satisfied all the conditions imposed on his licence and has discovered oil in commercial quantities (i.e. production of at least 10,000 barrels of oil per day from the licensed area).[21] The holder of an OML, in addition to virtually having all other rights of a licensee of an OPL, has the exclusive right to search for, win, work, carry away and dispose of all the petroleum discovered and won in the area covered by the lease. The term of an OML shall not exceed twenty years, but may be renewed on an application made to the Minister of Petroleum Resources not less than twelve months before the expiration of the lease. The renewal shall be granted if the lessee has paid all rent and royalties due and has also performed all his obligations under the lease.

In addition to the above requirements, there are other general requirements imposed on the holders of OELs, OPLs and OMLs. These include the furnishing of the following:[22]

(i) Ten copies of a map in respect of the area in which the application is made;

(ii) evidence of the financial status and technical competence of the applicant;

(iii) details of work which the applicant is prepared to undertake or a programme for carrying out any minimum working obligations imposed;

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[21] Contrast with the "significant discovery licence" (SDL) and the "production licence" (PL) under section 2 of the CPRA. A significant discovery is defined as: "A discovery indicated by the first well on a geological feature that demonstrates by flow testing the existence of hydrocarbons in that feature and, having regard to geological and engineering factors, suggests the existence of an accumulation of hydrocarbons that has potential for sustained production" and a commercial production (which is related to the PL) is defined as: "a discovery of petroleum that has been demonstrated to contain petroleum reserves that justify the investment of capital and effort to bring the discovery to production."

[22] See Part 1 of the *Petroleum (Drilling and Production) Regulations* of 1969. This Regulations were made pursuant to the powers granted to the Minister of Petroleum Resources by section 8 of the Act. [Hereinafter Regulations].

(iv) details of the annual expenditure which the applicant is prepared to make on each area applied for;

(v) the date on which it is prepared to begin operations after the grant of the OEL, OPL or OML to which the application relates;

(vi) details of a specific scheme for the recruitment and training of Nigerians;

(vii) evidence of the applicant's ability to market any petroleum produced;

(viii) annual reports in respect of the applicant's oil exploration and production activities in the preceding three years; and

(ix) any other information which the Minister may call for by notice in the federal gazette or otherwise.

A licence or lease may be granted only to a citizen of Nigeria, or a company incorporated in Nigeria under the *Companies Act* of 1968 or any corresponding law. Most of the OMLs existing in 1969 had been granted under the repealed *Mineral Oils Ordinance* of 1914. The duration of the maximum primary term of an OML under the Act is twenty years, but the subsisting OMLs granted under the repealed Ordinance were for primary terms of thirty and forty years. The question has, therefore, arisen as to whether OMLs granted under the repealed Ordinance for thirty and forty years are deemed to have been reduced to a term of twenty years.[23] It has been submitted that, as a result of the transitional and saving provision of the Act, as well as the universally accepted legal principle of sanctity of contract, the duration of OMLs granted under the repealed Ordinance before November 27, 1969 cannot be validly reduced.[24] This latter view is suspect. The legal principle of sanctity of contract cannot be used to justify the continued existence of OMLs granted under the repealed Ordinance. It is specifically provided in the pre-1969 OMLs granted by the government that:[25]

> It shall be governed by and construed in accordance with the laws of Nigeria and Nigerian law shall be the proper law....

It follows, therefore, that since the proper law of the contract is Nigerian law, the government by an exercise of its legislative sovereignty can modify or discharge its contractual obligations by altering the proper law; for example, by reducing the primary term of an OML from thirty years to twenty years. If the matter is looked according to the principles of the conflict of laws, there can be no doubt that the proper law, as determined by the private international law of the forum, "not merely sustains but, because it sustains, may also modify or dissolve the contractual bond."[26] The Act, however, protects OMLs granted under the repealed Ordinance by virtue of the transitional and saving provision contained in schedule 4 of the Act. It provides that:

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[23] See M. Kassim-Momodu, "Duration of Oil Mining Leases in Nigeria" (1988) 6 J.E.N.R.L. 103 at 104. Kassim-Momodu says that this appears to be the view of the Nigerian National Petroleum Corporation (NNPC). This view is also supported by O. Lolomari, "The Evolution of Nigerian Oil Policy" in *Oil and the New International Economic Order*, Proceedings of the 1976 Annual Conference of the Nigerian Economic Society (Ibadan: The Nigerian Economic Society, 1976), 13 at 15, where the writer, while commenting on the 1969 Act submits that: "Making the usual noises about the sanctity of contract, the companies only grudgingly accepted the new Decree (Act) which among other things, reduced the initial duration of leases from thirty to twenty years."

[24] Kassim-Momodu, *ibid.*

[25] See *Article* 60 of Model OML for continental shelf areas in *Basic Oil Laws and Concession Contracts, South and Central Africa (Original Text), Supplement* Nos. 1-5.

> Any licence or lease granted under an enactment repealed by this Act shall continue in force notwithstanding the repeal, but shall be subject to this Act and to any regulations made thereunder except as regards the duration of the licence or lease, the rent and royalties payable in respect thereof....

The above provision adequately protects the duration of pre-1969 OMLs granted under the repealed Ordinance.[27] There is, therefore, no justification for relying on the legal principle of sanctity of contract.[28]

2.2.d. Rights and Powers of holders of OPLs and OMLs

The rights and powers of holders of OPLs and OMLs are provided for in

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[26] R. Brown, "Choice of Law Provisions in Concession and Related Contracts" (1976) Mod.L.R. 625 at 633. According to Brown at 639, positions taken on the issue of sanctity of contract are only marginally relevant to a situation in which the parties make, in the first instance, express reference to a municipal law system, characteristically, of course, to the law of the host state.

[27] See also G. Utomi, "Special Report on Nigeria" April 1991 Special Supplement I.F.L. Rev. 58 at 60. He argues that OMLs granted prior to the Act are saved by the transitional provision. A saving provision is also contained in section 110(1) of the CPRA. It provides that where an exploration agreement was entered into or negotiations thereunder were completed under the old Canada Oil and Gas Act (now repealed), the exploration agreement will be treated like an exploration agreement under the new Act.

[28] The principle of "sanctity of contract" was relied on by the arbitrator in *Texaco Petroleum Company Ltd. and California Asiatic Oil Company* v. *The Government of Libya* (1979) 53 I.L.R. 389. The arbitrator held that the concession constituted a binding obligation under international law and that, according to the 'principle of sanctity of contract', Libya was bound to respect its contractual engagement. However, a different view was expressed in *Libyan American Oil Company* v. *The Government of Libya* (1981) I.L.M. 1 and *British Petroleum Company* v. *The Government of Libya* (1974) 53 I.L.R. 297. In the above cases, the arbitrators relied on the resolution establishing the New International Economic Order of May 1 1974 as supporting the sovereign rights of states to control and ownership of their natural resources.

Part III of the Regulations. These rights are subject to all the applicable laws and to the approval in writing of the Head of the Department of Petroleum Resources and of other appropriate government agencies and to such conditions as they may impose. These rights and powers include:[29]

(a) To cut down and clear timber and undergrowth;

(b) to make roads;

(c) to appropriate and use water found in relevant area and to collect and impound the same, but so that in the exercise of this right the licensee or lessee shall not deprive any lands, villages, houses or watering places for cattle of a reasonable supply thereof or interfere with any rights of water enjoyed by any person under the Land and Native Rights Act or any other enactment;

(d) to construct, bring, maintain, alter, operate, dismantle or remove -

(i) industrial buildings and installations, including drilling platforms, engines, power plants, flowlines, storage tanks, loading terminals, harbours, jetties, piers, moles, landing places and derricks;

(ii) means of communication, including telephones lines and wireless stations;

(iii) facilities for shipping and aircraft;

(iv) living accommodation and amenities for the employees and workmen

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[29] See part III of the Regulations. A similar provision was contained in pre-1969 grants. See *Article* 2 of Model OPL for land and territorial waters areas and *Article* 3 of Model OML for continental shelf areas in *Basic Oil Laws and Concession Contracts, South and Central Africa (Original Text), supra*, note 25.

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(d) to construct, bring, maintain, alter, operate, dismantle or remove -

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(ii) means of communication, including telephones lines and wireless stations;

(iii) facilities for shipping and aircraft;

(iv) living accommodation and amenities for the employees and workmen of the licensee or lessee; and

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[29] See part III of the Regulations. A similar provision was contained in pre-1969 grants. See *Article* 2 of Model OPL for land and territorial waters areas and *Article* 3 of Model OML for continental shelf areas in *Basic Oil Laws and Concession Contracts, South and Central Africa (Original Text)*, *supra*, note 25.

(v) other buildings, installations, works, chattels and effects;

(e) to dredge;

(f) to search for, dig and get free of charge gravel, sand, clay and stone not subject to any licence or lease within unoccupied state land provided it is not sold, and on completion of work all excavations shall be filled or levelled out to the satisfaction of the Head of the Petroleum Inspectorate.

The licensee or lessee is not authorized to enter land which is sacred, until permission in writing has been obtained from the Minister and fair and adequate compensation paid to the persons in lawful occupation of the land.[30]

2.2.e. Assignment of an OPL or OML

The assignment of an OPL or OML without the prior consent of the Minister of Petroleum Resources is prohibited under paragraph 14 of schedule 1 of the Act.[31] Under paragraph 15, the prescribed fee shall be paid on an application for an assignment under paragraph 14 and the Minister's consent for the assignment may be given on payment of such other fee or such premium or both and upon such terms as the Minister may decide. The Minister may however, waive payment of that other fee or that premium, or both, if he is satisfied that the assignment is to be made to a company in a group of which the assignor is a member, and is to be made for the purpose of reorganization in order to achieve greater efficiency and to acquire resources for more effective petroleum operations.

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[30] On compensation see G. Etikerentse, "The Impact of the 1978 Land Use Act on Land Acquisition Compensation" (1984-85) 3 O.G.L.T.R. 72 and M. Kassim-Momodu, "The Impact of the Land Use Act on Petroleum Operations in Nigeria" (1990) 8 No. 4 J.E.N.R.L. 291.

[31] For pre-1969 grants, see *Article* 45 of Model OPL for land and territorial waters areas and *Article* 49 of Model OML for continental shelf areas in *Basic Oil Laws and Concession Contracts, supra*, note 25.

The Minister shall not give his consent to an assignment unless he is satisfied that:[32]

(a) The proposed assignee is of good reputation, or is a member of a group of companies of good reputation or is owned by a company or companies of good reputation;

(b) there is likely to be available to the proposed assignee (from its own resources or through other companies in the group of which it is a member or otherwise) sufficient technical knowledge and experience and sufficient financial resources to enable it effectively to carry out a programme satisfactory to the Minister in respect to operations under the licence or lease which is to be assigned; and

(c) the proposed assignee is in all other respects acceptable to the federal government.

By virtue of the above provisions, any assignment of an OPL or an OML in or outside Nigeria without the prior approval of the Minister of Petroleum

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[32] Schedule 1, paragraph 16 of the Act.

Resources is ineffectual.[33] It could be argued that the above restriction on the assignment of OPLs or OMLs does not apply, for example, where a change in ownership occurs.[34] In other words, it is not an assignment for Company 'A' to acquire the equity shares of Company 'B'. This argument is based on the distinction between the words "assign" and "acquire." An "assignment is the act of transferring to another all or part of one's property,....interest, or rights...."[35] On the other hand, an "acquisition is the act of becoming the owner of certain property; the act by which one acquires or procures the property in anything...."[36]

An argument against this position may take the following form. It is a cardinal rule of statutory interpretation that in construing statutes and written instruments, words must be understood in their natural and ordinary sense (the literal rule of interpretation), unless this would lead to some absurdity or inconsistency with the rest of the instrument.[37] In order to prevent absurdity or inconsistency, the word "assignment" must be given its widest meaning to include "acquisition." The Department of Petroleum Resources of the Ministry of Petroleum, which regulates and supervises operations under licences or leases does not however, differentiate between transfer by "assignment" of licences or leases and the "acquisition" of the equity shares in the operating company whether involving a change of control of the lessee or licensee country of origin.[38]

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[33] G. Oyebode, "Government Regulatory Approval Processes in Nigeria" [1990] Energy Law 743 at 745.

[34] *Ibid.* at 745-746.

[35] Black's Law Dictionary 6th ed., (St. Paul, Minnesota: West Publishing Co., 1990) at 119.

[36] *Ibid.* at 24.

[37] F. Bennion, *Statutory Interpretation* (London: Butterworths, 1984) at 657-668, P.St.J. Langan, *Maxwell on the Interpretation of Statutes* 12th ed., (London: Sweet & Maxwell, 1969) at 43 and also *Becke* v. *Smith* (1836) 2 M. & W. 191 at 195, *per* Parke B.

We may, therefore, conclude that although an "acquisition" is not the same as an "assignment" in law, the Department of Petroleum Resources of the Ministry of Petroleum Resources in practice treats an "acquisition" of equity shares in the same way as an "assignment."

2.2.f. Revocation of an OPL or OML

The causes for which an OPL or OML may be revoked by the Minister of Petroleum Resources are contained in paragraph 23(1) of Schedule 1 of the Act. Under this paragraph, the Minister may revoke any OPL or OML if the licensee or lessee becomes controlled directly or indirectly by a citizen or subject of, or a company incorporated in, any country which is:[39]

> (a) A country other than the licensee's or lessee's country of origin, and
>
> (b) a country the laws of which do not permit citizens of Nigeria or Nigerian companies to acquire, hold and operate petroleum

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[38] Oyebode, *supra*, note 33 at 746.

[39] An identical provision can be found in the pre-1969 grants. See *Articles* 41 & 42 of Model OPL for land and territorial waters areas and *Articles* 45 & 46 of Model OML for the continental shelf areas in *Basic Oil Laws and Concession Contracts supra*, note 25

> concessions on conditions which in the opinion of the Minister are reasonably comparable with the conditions upon which such concessions are granted to subjects of that country.

In addition, under paragraph 24 of schedule 1 of the Act, the Minister may revoke any OPL or OML if in his opinion the licensee or lessee:

> (a) Is not conducting operations continuously and in a vigorous and businesslike manner and in accordance with good oil field practice, or
>
> (b) has failed to comply with any provision of this Act or any regulation or direction given thereunder or in fulfilling his obligations under the special conditions of his licence or lease, or
>
> (c) fails to pay his due rent or royalties, whether or not they have been demanded by the Minister within the period specified by or in pursuance of this Act, or
>
> (d) has failed to furnish such reports on his operations as the Head of the Petroleum Inspectorate may lawfully require.

If the government decides to revoke any licence, it shall inform the licensee or lessee of the grounds on which the revocation is contemplated and shall invite the licensee or lessee to make any explanation if it so desires.[40] If the government is satisfied with the explanation, it may invite the licensee or lessee to rectify the matter complained of within a specified period.[41] If the licensee or lessee makes no sufficient explanation, or does not rectify the matter complained of within the specified period, the Minister may revoke the licence or lease.[42]

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[40] Schedule I, paragraph 25 of the Act.

The notice of revocation is then published in the federal government official gazette, but the licensee or lessee remains liable for all obligations incurred before the effective date of such revocation.[43] The effectiveness of this power of revocation has been questioned by Etikerentse. He argues that:[44]

> The importance attached to the revocation powers of the grantor in this matter has been eroded to a great extent by the very fact that in nearly all petroleum operations in Nigeria now, the Government through NNPC has participation interests. NNPC's representatives have a say in the way the operations are carried out and they would therefore be privy to any defaults deserving of revocation. A revocation would thus affect both parties to the joint venture and the NNPC's inspectorate, being the actual organ charged with effecting any revocation, would be most reluctant to carry out a measure that would indirectly affect its *alter ego.*

The above assertion illustrates one of the disadvantages of equity participation. As a controlling shareholder in the subsidiaries of the IOCs, the government can hardly be expected to effectively exercise its power of revocation of the licences and leases held by the oil companies.

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[41] *Ibid.*, paragraph 26.

[42] *Ibid.*, paragraph 27.

[43] *Ibid.*, paragraphs 28 & 29.

[44] *Supra*, note 3 at 38-39.

If, for example, Texaco International, (a company incorporated in the United States), indirectly controls Texaco Nigeria PLC, (a subsidiary company) through its control of the management of the Nigerian subsidiary, one would expect that the requirement of paragraph 23(1)(a) of schedule 1 of the Act would have been met and if the requirement of paragraph 23(1)(b) is also satisfied, the government's power of revocation would be activated. However, it will be counter-productive for the government to revoke Texaco's licences or leases, since it holds sixty per cent (60%) equity shares in the company. This example shows that equity participation was implemented without careful consideration of particular facts. Although this control imposed by the Act is reasonable and is meant to prevent companies which are not acceptable to the government from taking over control of the IOCs operating in Nigeria, its effectiveness, for the reason given above, is doubtful.[45]

2.2.g. A Comparison of the pre-1969 Grants with Grants made under the Act

A comparison of the pre-1969 grants of oil rights with grants made under the Act reveals that the Act incorporates all the salient provisions of the previous laws under which pre-1969 grants of oil rights were made.[46] For example, the provisions relating to assignment, revocation, the rights and powers of the holders of OPLs and OMLs, which were considered above under the Act, were also dealt with in the pre-1969 grants of oil rights. This has led one writer to conclude that:[47]

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[45] Oyebode, *supra*, note 33 at 746.

[46] Etikerentse, *supra*, note 3 at 24.

> The Petroleum Act, to which much economic hope had been pinned, proved to be hollow, in that apart from the reduction in the primary term of an oil-mining lease to twenty years for new grants as compared to earlier grants for thirty and forty years no worthwhile changes in the rights of the transnational concessionaries had taken place in Nigeria's favour. It was discovered that Nigeria's financial derivations from petroleum had not increased to any appreciable extent.

This criticism has some merit. Although the Act laid the foundation for subsequent developments in Nigeria's oil industry with the introduction of equity participation, in terms of *de facto* control of the oil industry, the Act did not make a fundamental change from the pre-1969 grants of oil rights.

One of the innovations introduced by the Act was the reduction of the duration of the term of an OML. Under the pre-1969 grants of oil rights, a distinction existed between OML for land and territorial waters areas and those issued in respect of continental shelf areas.[48] The former were granted for thirty years with the lessee having the option to renew for another thirty years period, while in the latter, OMLs were issued for forty years with the option for the lessee to renew for a further period of forty years.[49] The terms and conditions applicable to the renewed OML were stipulated to be the same as those of the existing OML, except for the renewal provisions.[50] Thus, a renewal does not carry a further right of renewal. The renewal of an OML under the pre-1969 grants of oil rights was subject to the lessee giving the Minister of Petroleum Resources not less than three months notice in writing of his intention to renew the lease. Before an OML is renewed, the lessee must have duly paid rent, royalties and petroleum profit tax in respect of its operations and must also have performed all of its obligations under the expiring OML.[51]

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[47] *Ibid.* at 12.

[48] *Ibid.* at 36. See section 1.3.b.iii. of chapter 1.

[49] Etikerentse, *ibid.*

[50] *Ibid.*

Unlike the pre-1969 grants of oil rights, the Act makes no distinction between OMLs covering land and territorial waters and those in respect of the continental shelf areas. Instead, paragraph 10 of schedule 1 of the Act provides that the term of an OML shall not exceed twenty years, but may be renewed in accordance with this Act. The lessee of an OML is entitled to apply in writing for a renewal of the lease, on condition that not less than twelve months notice of the intention to renew is given to the Minister and the lessee must have paid the rent, royalties, and performed the obligations imposed on the lease. Surprisingly, the Act does not provide for the number of years to which a lessee would be entitled on renewal of the expiring lease. It has been submitted that, the period of renewal must presumably be left to the Minister's discretion.[52] It could, however, be argued that since the maximum term of an OML under the Act is twenty years, then, the period of renewal may also be twenty years.

Under paragraph 12(1) of schedule 1 of the Act, ten years after the grant of an OML, one-half of the area of the lease shall be relinquished. This relinquishment provision was not present in the pre-1969 grants of oil rights. The question has, therefore, arisen as to whether the relinquishment provision of the Act applies to the pre-1969 grants of oil rights even in the face of the transitional and saving provision of schedule 4 of the Act. Since the saving provision applies to duration, rent and royalties, it follows that the duration, rent and royalties of the pre-1969 grants of oil rights cannot be validly altered. We can, therefore, conclude that the pre-1969 OMLs are not subject to the relinquishment provision contained in paragraph 12(1) of schedule 1 of the Act.[53] To hold otherwise would amount to a reduction of the duration of the primary term of an OML granted under the pre-1969 grants of oil rights and, thus, a derogation from the rights which are saved by the saving provision of the Act.[54]

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[51] *Ibid.*

[52] *Ibid.*

The relinquishment provision was however, one of the innovations introduced by the Act and its importance cannot be overemphasised. It encourages rapid exploration and development of the oil industry by the IOCs. The IOCs knowing that one-half of the area of the lease shall be relinquished after ten years, would speed up their exploration activities.

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[53] *Ibid.* at 37.

[54] *Ibid.*

2.2.h. The Nature of the Interest Granted under the Act

The nature of the interest granted to a licensee or lessee under the Act has not occasioned much controversy because it is clearly defined in the Act and Regulations.[55] An OEL confers on the licensee the right to explore for petroleum.[56] This right is, however, not exclusive to the licensee as another OEL may be granted over the same area. In addition, the licensee may only undertake aerial and surface geological and geophysical surveys, excluding drilling below 91.44 metres. On the other hand, an OPL confers on the licensee the right to explore, carry away and dispose of petroleum discovered and won in the area covered by the licence. This right is exclusive so that another OPL may not be granted in respect of the same area.[57] The holder of an OPL can, therefore, by private action, exclude another oil company from its area of operation.

Similarly, an OML confers on the lessee the right to explore, carry away, and dispose of petroleum discovered and won in the area covered by the lease.[58] Unlike a normal lease, an OML granted under the Act does not create an estate in land *per se.* [59] It is in the nature of a mineral lease which permits the lessee to use the land to explore and dispose of any petroleum discovered within the leased area (i.e. a *profit a prendre*). Thus, the actual rights conferred by an OML are limited to the interests in the petroleum discovered in the sub soil of the leased area.[60] In the next section, we examine the nature of equity participation which was the major innovation introduced by the Act.

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[55] In Canada the nature of the oil and gas lease has been a nightmare for the judiciary. In *Re Heier Estate* (1952-53) 7 W.W.R. (N.S.) 385, the Saskatchewan Court of Appeal held that the so called oil and gas lease under review is a sale of a portion of the land in the form of petroleum and natural gas within, upon or under the said land. In 1957 the Supreme Court of Canada in *Berkheiser* v. *Berkheiser* [1957] S.C.R. 387, 7 D.L.R. (2d) 721, brought some sanity into this area of the law and held that an oil and gas lease conferred on the lessee a *profit a prendre*. See however, *Hayes* v. *Mayhood* [1959] S.C.R. 568, 18 D.L.R. (2d) 497, where the Supreme Court of Canada held that an oil and gas lease was a lease for the purposes of the Alberta *Devolution of Real Property Act*. See Ballem, *supra*, note 18 at 12-19. In the United States of America, the nature of the interest acquired under an oil and gas lease varies from one jurisdiction to another. In Texas, a lessee of an oil and gas lease acquires a determinable fee, while in Pennsylvannia, ownership of oil and gas is not recognised until it is captured and reduced into possession. See H.R. Williams & C.J. Meyers, *Oil and Gas Law* (New York: Matthew Bender, 1991) at 33-50.

[56] Schedule 1, paragraphs 1-4 of the Act.

[57] *Ibid.*, paragraphs 5-7. According to Etikerentse, *supra*, note 3 at 25, OELs or OPLs are basically not different from the ordinary licence.

2.3. Equity Participation

National participation in the international oil industry is not a new phenomenon.[61] Participation is a partnership arrangement wherein the state, either directly or through its national oil company (NOC), receives an equity or ownership interest in the rights and obligations of a contract or a concession.[62] In major oil producing countries today, the state-owned oil corporations have been established to function as instruments for achieving effective government participation in the oil industry.[63] The objectives of state participation include:

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[58] Schedule 1, paragraph 11 of the Act.

[59] Etikerentse, *supra*, note 3 at 27.

[60] This interpretation is in line with the decision of the Supreme Court of Canada in *Berkheiser* v. *Berkheiser*, *supra*, note 55, Rand J. for himself and Cartwright J. said at 392: "...I interpret it as either a *profit a prendre* or an irrevocable licence to search for and win the substances named...." Kellock J.(for himself, Locke and Nolan JJ.), said at 395: "...In my opinion, the instrument is to be construed as a grant of a *profit a prendre* for an uncertain term which might be brought to an end upon the happening of any of the various contingencies for which it provides...." A *profit a prendre* is an incorporeal interest in land authorizing entry upon a tract of land and the severance and removal of a part of the corpus of the land. See H.R. Williams & C.J. Meyers, *Manual of Oil and Gas Terms* (New York: Matthew Bender & Co., 1984) at 688.

[61] K. Adeniji, "State Participation in the Nigerian Petroleum Industry" (1977) 11 J.W.T.L. 156 at 156. See also P.H. Frankel, "The Rationale of National Oil Companies" in United Nations ed., *State Petroleum Enterprises in Developing Countries* (London: Pergamon Press, 1980), 3 at 3-4.

(i) To increase the HC's share of the earnings of the oil industry;[64]

(ii) to give the HC a voice in the policy decisions of the company and to exercise *de facto* control over the oil industry;[65] and

(iii) to develop technical and managerial skills in the oil industry.[66]

In 1960, OPEC was formed with the tilting of the erstwhile contractual equilibrium in favour of its member nations as its primary objective.[67] OPEC, at its XV1 Conference of June 1968, passed resolution No.90, which called for modifications in the structure of the contractual relationship between OPEC member states and the IOCs.[68] It provided that:[69]

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[62] G.H. Barrows, *World Wide Concession Contracts and Petroleum Legislation* (Tulsa, Oklahoma: Pennwell Publishing Co., 1983) at 28. Participation could be equity or non-equity. Equity participation is usually by a majority share holding of the state or its national oil corporation (also referred to as equity joint venture). Non-equity participation is the joint venture type agreement between the government and the oil companies. Contractual joint ventures will be discussed in chapter 3.

[63] Adeniji, *supra*, note 61 at 157.

[64] *Ibid*. at 159. See also Ajomo, *supra*, note 2 at 93.

[65] Adeniji, *ibid*. See also P. McPherson, "Recent Developments in Petroleum Laws and Contracts" [1984] International Energy Law 33 at 45 and Ajomo, *ibid*. at 92-93.

[66] Adeniji, *ibid*. and Ajomo, *ibid*. at 92.

[67] Etikerentse, *supra*, note 3 at 11.

[68] Adeniji, *supra*, note 61 at 157. See also H.S. Zakariya, "Sovereignty, State Participation and the Need to Restructure the Existing Petroleum Concession" (1971) 10 Alta. L.R. 218 at 223.

> Where provision for government participation in the ownership of the concession-holding company under any of the present petroleum contracts has not been made, the government may acquire a reasonable participation, on the grounds of the principle of changing circumstances....[70]

At the time this resolution was passed in 1968, the Nigerian government had no equity share in any of the subsidiary oil companies operating in Nigeria, neither was Nigeria a member of OPEC. However, the policy of participation advocated in OPEC resolution 90, featured prominently in Nigeria's National Development Plan, 1970-1974.[71] According to Ajomo:[72]

> The country had, by the beginning of the seventies, come to realise that the concept of permanent sovereignty over natural resources must be vigorously asserted as a *sine qua non* of national independence and economic self sufficiency. One way of asserting this independence was either nationalisation/ expropriation or to achieve the same goal through the adoption of the less drastic strategy of acquiring equity interest in the producing company. Nigeria chose the latter as a better substitute for nationalisation.

In addition, the Act had laid the foundation for state participation in the oil industry.[73] Under paragraph 34 of schedule 1 of the Act, it is provided that

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[69] See *OPEC Official Resolutions and Press Releases*, *supra*, note 15 at 62.

[70] This resolution was affirmed in 1971. See Resolution 135 of July 1971 in *OPEC Official Resolutions and Press Releases ibid.* at 89.

[71] Ajomo, *supra*, note 2 at 90.

[72] *Ibid.*

[73] Equity participation had however been thought of as far back as 1962 in a concession agreement between the government and Nigerian Agip Oil Company, in which the government was granted an option to acquire 30% equity interest in the company. See M.M. Olisa, *A Comparative Study of the Acquisition of Oil and Gas Rights in Africa* (Edmonton, Alberta: University of Alberta, LL.M Thesis 1967, Unpublished) at 58 & 67.

the Minister of Petroleum Resources if he considers it to be in the public interest, may impose on a licence or lease terms and conditions as to participation by the federal government in the venture to which the licence or lease relates, on terms to be negotiated between the Minister and the applicant for the licence or lease.

After Nigeria joined OPEC in July 1971,[74] and in compliance with OPEC's time-table which required each member country to acquire fifty one per cent (51%) participating interest in the subsidiaries of the IOCs by April 1 1982, the government started negotiations with the IOCs. The reason given for the government's participation in the oil industry was that oil was going to play a strategic role in the nation's economy.[75] Government participation was, therefore, a political as well as an economic necessity.[76] This was achieved through negotiations with the IOCs (except in the case of Elf).[77] The Nigerian government's participation was effected through its state-owned oil corporation, the NNPC. Under equity participation, the state-owned corporation acquires certain interest percentage in the operations of the IOCs.[78]

In 1971, the federal military government revoked the OPLs formerly granted to Elf and which were due for renewal, and took thirty five per cent (35%) equity interest in its Nigerian subsidiary.[79] In the same year, the government also exercised an option that existed in a 1962 concession agreement with Nigerian Agip Oil Company and took 33 1/3% equity interest in the company.[80] Although this was an isolated agreement providing for state participation, its terms indicate that participation had been thought of as early as 1962. This appears to have been prompted by the fact that:[81]

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[74] Resolution 134 of July 1971 in *OPEC Resolutions and Press Releases*, *supra*, note 15 at 89.

[75] Adeniji, *supra*, note 61 at 160.

[76] *Ibid.* at 161.

[77] *Ibid.*

[78] Etikerentse, *supra*, note 3 at 13. See also K.W. Blinn et al, *International Petroleum Exploration and Exploitation Agreements - Legal, Economic, and Policy Aspects* (New York: Barrows Co., Inc., 1986) at 99-100.

> Participation is seen by the state to offer more scope than the conventional concession for generating domestic capital, and providing technical and managerial skills.

The government also successfully negotiated a participation agreement with Shell-BP in which the government took thirty five per cent (35%) equity interest in its Nigerian subsidiary. The agreement became effective from April 1 1973.[82] Negotiations with the other IOCs followed suit and by April 1 1974 the government had acquired fifty five per cent (55%) participating interest in the subsidiaries of the IOCs operating in Nigeria.[83] By April 1 1979, after prolonged negotiations with the IOCs, the government's participating interest in the subsidiaries of the IOCs increased to sixty per cent (60%). The government also held sixty per cent (60%) participating interest in Shell-BP, but in the fourth quarter of 1979, the government nationalized BP's twenty per cent (20%) shares in Shell-BP. Thus, until 1989, the government held eighty per cent (80%) participating interest in Shell.[84]

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[79] Ajomo, *supra*, 2 at 91. According to Ajomo, the reason for the revocation and subsequent acquisition of 35% equity interest in Elf was because of the surreptitious support which the French government gave to "Biafra" during the Nigerian civil war 1967-1970. See also Lolomari, *supra*, note 23 at 21.

[80] Ajomo, *ibid*. This option to participate was to the extent of 30%, but when it was exercised in 1971, the government took 33 1/3%. See Lolomari, *ibid*.

[81] Olisa, *supra*, note 73 at 67.

[82] Ajomo, *supra*, note 2 at 91.

[83] *Ibid*. See also (1974) June Vol.XLI No.6, The Petroleum Economist at 212 and T. Turner, "Nigeria: Imperialism, Oil Technology and the Comprador State" in P. Nore & T. Turner, *Oil and Class Struggle* (London: Zed Press, 1980), 199 at 209.

Equity participation led to an increase in revenue for the government; and participation in the downstream operations such as refining, marketing, and distribution.[85] The main objective of equity participation according to the government, is to secure *de facto* control and sole responsibility for resources development, using the IOCs primarily as a contributing agent.[86] In the concluding section of this chapter, it will be argued that this objective has not been achieved as *de facto* control of the oil industry is still in the hands of the IOCs. The joint venture relationship between the NNPC and the IOCs has the following features:[87]

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[84] See the Acquisition of Assets *(British Petroleum Company Limited) Act* 1979 (No.56 of 1979), referred to in Ajomo, *ibid.* at 92. The nationalization of BP's assets in Nigeria was a political move against the British government's widely publicised decision to supply crude oil to South Africa. See Ajomo at 92 n.22. In 1989, the government voluntarily relinquished part of its eighty per cent (80%) interest in Shell to establish the present partnership structure of NNPC sixty per cent (60%), Shell Petroleum Development Company thirty per cent (30%), Elf Nigeria five per cent (5%) and Nigerian Agip Oil Company five per cent (5%) in the NNPC/Shell joint ventures. See (1991) September/October Report No.138, World Petroleum Taxation and Legislation at 51.

[85] R. Kemper, "The Concept of Permanent Sovereignty and its Impact on Mineral Contracts" in *Legal and Institutional Arrangements in Minerals Development* (London: Mining Journal Books, 1982), 29 at 32-33.

[86] *Ibid.* See also Lolomari, *supra*, note 23 at 22 and (1974) February Vol.XLI No.2, The Petroleum Economist at 58.

2.3.a. The Participation Agreement

This is negotiated on an individual basis and specifies the respective rights of the parties; NNPC's participating interest in the OML; the fixed and moveable assets of the oil company in Nigeria such as exploration, development, production, transport storage, delivery facilities and export operations and assets such as offices, houses etc; the working capital relating to the operations of the OML including materials, stocks and assets etc.

2.3.b. The Operating Agreement

This is signed by the joint venture partners and it spells out the legal relationship between the partners. It also lays down the rules and procedure for the joint development of the areas concerned and of the property jointly owned by the partners; i.e. expenditure for practically all activities and services of the oil company. The operator under an operating agreement is responsible for the conduct of all joint venture operations and is subject to the supervision and control of a committee comprising representatives of the joint venture partners.

An example of an operating agreement is that signed in July 1991 between the Minister of Petroleum Resources with NNPC's partners in the NNPC/Shell joint ventures.[88] The joint venture partners are NNPC sixty per cent (60%), Shell Petroleum Development Company thirty per cent (30%), Elf

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[87] Utomi, *supra*, note 27 at 59-61 and Y. Omorogbe, "The Legal Framework for the Production of Petroleum in Nigeria" (1987) 5 No. 4 J.E.N.R.L. 273 at 278-279.

[88] See World Petroleum Taxation and Legislation Report, *supra*, note 84 at 51.

Nigeria five per cent (5%) and the Nigerian Agip Oil Company five per cent (5%). Shell is the operator of the joint ventures.[89] Prior to the signing of the operating agreement in July, no formal operating agreement existed between the partners.[90] The agreement signed in July was, thus, the first operating agreement to formalize the working relationships between the joint venture partners.

2.3.c. The Memorandum of Understanding (MOU)

In 1986, the NNPC signed with each oil company a MOU.[91] This is a fiscal measure designed to guarantee high production and lifting volumes and a minimum steady profit margin of US $2.00 per barrel for prices between US $12.50 - U.S. $23 and for prices under U.S. $12.50 a guaranteed profit margin in accordance with a specified formula and US $1.00 per barrel on emergency crude. This was aimed at stimulating exploration and production activities.

The oil companies under the MOU committed themselves to specified minimum exploration, production and development work programmes. They also undertook to lift certain volumes of NNPC's equity share of crude oil which it is unable to lift. There are penalties for non performance - for example, there is a specified amount payable for every unlifted barrel and failure to comply with the work obligations attracts a denial of the fiscal conditions under the MOU.[92]

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[89] *Ibid.*

[90] *Ibid.*

[91] This came into effect on January 1, 1986.

2.3.d. The Heads of Agreements

These lay down guidelines for the sharing of production. They provide, *inter alia*, for undivided interests in the rights granted in respect of petroleum in the area and specify that each interest owner can only lift as much as its participating share.

There are other types of contractual arrangements apart from equity participation for oil exploration and production which do not arise from the grant by the Minister of OELs, OPLs or OMLs.[93] These will be discussed in chapter 3.

2.3.e. An Assessment

The above description of the different modes of acquisition of oil rights reveals that the Act maintains the basic framework of the pre-1969 grants of oil rights. Since equity participation was the major innovation introduced by the Act, it is imperative that an assessment should focus on equity participation in order to determine whether it achieves the objectives of the government. The main objectives of the Nigerian government in implementing equity participation include:[94]

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[92] On May 23, 1991 the federal government issued a press release on allocation of new acreage for oil exploration and production in Nigeria, and a revision of the MOU between the government and the IOCs. See World Petroleum Taxation and Legislation Report, *supra*, note 84 at 52-53.

[93] Etikerentse, *supra*, note 3 at 42 and Omorogbe, *supra*, note 87 at 277-291.

(i) To increase the government's revenue from the oil industry;

(ii) the acquisition of the necessary technological and managerial skills for petroleum development; and

(iii) to achieve *de facto* control of the oil industry.

Equity participation has no doubt led to a substantial increase in the government's revenue [95] thereby furthering the government's objective of rapid industrial development. It must however, be stressed that equity participation was not always motivated by the objectives outlined above. For example, the government's acquisition of thirty five per cent (35%) equity shares in Elf in 1971 and the nationalization of BP's twenty per cent (20%) shares in Shell-BP, were motivated by political considerations.

In addition, the government's objectives could have been effectively secured by other means which do not involve the acquisition of controlling equity shares in the subsidiaries of the IOCs. The government's revenue from the oil industry could have been increased by increasing the rents, royalties and premiums payable to it by the oil companies while still maintaining the pre-1969 framework for the acquisition of oil rights. Similarly, the necessary technology could have been acquired by the government through other avenues, such as by entering into bilateral and co-operation agreements with other OPEC countries. Equity participation was however, one of the basic requirement of OPEC's resolution No.90 of June 1968, which required member countries to acquire a reasonable participation in their oil industry, on the grounds of the principle of changing circumstances. The implementation of equity participation by the Nigerian government in its oil industry must, therefore, be seen primarily, as a compliance with OPEC's directives.

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[94] The Petroleum Economist, *supra*, note 86 at 58 and (1975) January Vol.XLII No.1, The Petroleum Economist at 15.

[95] D.N. Smith, *New Eyes for Old: The Future, Present and Past in the Evolution of Mineral Agreements* (Lagos: Nigerian Institute of Advanced Legal Studies, 1981) at 15-16. The value of crude oil export in 1958 was 1.8 million naira. This rose to 40.4 million naira in 1963 and in 1974 it was 6.45 billion naira. Sources: Federal Office of Statistics Central Planning Office and Ministry of Petroleum Resources, referred to in S.B. Falagan & G.O. Okah, "The Contribution of Petroleum to the Nigerian Economy" in *Oil and the New International Economic Order supra*, note 23 at 188.

In terms of achieving *de facto* control of the oil industry, equity participation did not constitute a radical departure from the framework of the pre-1969 grants of oil rights.[96] Although the government now has a majority representation on the boards of the subsidiaries of the IOCs, *de facto* control still resides with the IOCs because they still retain effective control of management of the subsidiary oil companies. In the absence of *de facto* control of the oil industry by Nigerians, it is doubtful whether equity participation is compatible with the principle of permanent sovereignty over natural resources.[97]

De facto control involves the exercise of decision making powers in such vital operational and managerial matters as budget, expansion and development programmes, appointment of top management, pricing, marketing, declaration of dividends, borrowing, reorganization, procurement of equipment, and the integration of the undertaking with the developmental objectives of the government.[98] Thus, the proper test of the viability of any new arrangement purporting to vest control in the government is: Does the restructuring result in *de facto* control being vested on the board of directors and, thus, the power to make the crucial decisions on these specific matters ?[99]

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[96] Smith, *ibid.* at 17.

[97] See section 4.3. of chapter 4.

Despite the government's acquisition of majority equity shares in the subsidiaries of the IOCs and its majority representation on the boards of these companies, the government have been willing to entrust the management of the subsidiaries to the IOCs, apparently on the assumption that they can exercise *de facto* control solely through representation at the board level.[100] However, the formal demarcation of responsibilities between the board and the management is such that the board is sometimes relegated to a perfunctory role as far as key management issues are concerned.[101] The consequence of such an arrangement is that the managerial powers enjoyed by the IOCs prior to the introduction of equity participation is virtually intact.[102]

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[98] S.K.B. Asante, "Restructuring Transnational Mineral Agreements" (1973) 73 America J.I.L. 335 at 346.

[99] *Ibid.* at 346-347.

[100] *Ibid.* at 349. The government through its majority representation on the boards of the subsidiaries of the IOCs can however, influence investment and production policies, but day-to-day decision making is left to the companies. See (1976) January Vol.XLIII No.1, The Petroleum Economist at 12.

[101] Asante, *ibid.* See also Kachikwu, *supra*, note 13 at 177, where the author submits that: "Today the boards of most multinational companies remain only as instruments for rubber stamping decisions arbitrarily taken by the foreign investor or its parent company abroad."

The corporate structure of the IOCs further enhances their control of Nigeria's oil industry. Thus, although all IOCs operating in Nigeria must be registered in Nigeria as local companies,[103] the management may still continue to refer all major decisions - technical, managerial, or financial - to its parent companies in America or Europe.[104] The result is that the headquarters of the parent companies retain *de facto* control of the new arrangement, in which they are technically junior partners.[105] The government's quest for ownership and control of the oil industry may have led to the confusion between symbols and substance. A close scrutiny of the key management positions of the IOCs operating in Nigeria shows that Nigeria has not developed the capability to manage the oil industry.[106] *De facto* control, therefore, very rarely corresponds to the degree of equity ownership.[107]

Equity participation rests on the assumption that the supervisory powers exercised on the boards of the subsidiaries of the IOCs will suffice to ensure the exercise of *de facto* control of the oil industry.[108] It is doubtful whether *de facto* control can be effectively maintained in cases where management powers include such vital items as corporate planning in the short and medium term.[109] Where management is entrusted with the day-to-day running of the oil industry, it is difficult to see what standards of overall direction and supervision could be employed by the government (through the boards of directors of the subsidiary oil companies) which -being a new owner of the oil resources - have not had the opportunity to establish a record of corporate management in the oil industry.[110]

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[102] Asante, *ibid.* at 350. See also Turner, *supra*, note 83 at 215.

[103] See section 54(1) of the *Companies and Allied Matters Decree* of 1990.

[104] Asante, *supra*, note 98 at 350 and also Kachikwu, *supra*, note 13 at 177.

[105] Asante, *ibid.*

[106] M.S. Olorunfemi, "Managing Nigeria's Petroleum Resources" (1986) December/January OPEC Bulletin 24 at 25-26.

[107] S.K.B. Asante & A. Stockmayer, " The Evolution of Development Contracts: The Issue of Effective Control" in *Legal and Institutional Arrangements in Minerals Development supra*, note 85. at 58. See also Smith, *supra*, note 95 at 18.

It can be stated safely that *de facto* control has neither been furthered to any substantial degree through the mere use of equity participation replacing the traditional concession regime of the pre-1969 grants of oil rights; nor has it, in fact, been exercised to the full extent envisaged by the principle of permanent sovereignty over natural resources as canvassed internationally.[111] *De facto* control of the oil industry can only be effectively exercised if "sufficient and appropriate capacity for control exist" i.e. control over management.[112]

Far from denying any intention to maintain control, some IOCs contend that the global character of their operations is inherently incompatible with the surrender of control over any one of their affiliates scattered around the world.[113] Control, they argue, must be maintained to ensure overall efficiency and conformity with the general pattern of their global operations.[114] In their conception, therefore, the acquisition of a majority equity interest in a local subsidiary amounts to no more than participation in a global operation.[115]

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[108] Asante & Stockmayer, *ibid.* at 59.

[109] *Ibid.*

[110] *Ibid.* See also (1976) July Vol.XLIII No.7, The Petroleum Economist at 263.

[111] Asante & Stockmayer, *ibid.* at 60.

[112] *Ibid.*

This argument by the IOCs fails to take into account the fact that their objectives, expressed through the managements of the subsidiaries which they control, may sometimes conflict with the objectives of the government, expressed through the boards of directors of the subsidiary companies. If we accept the view of the IOCs of the need for them to maintain control of management of their subsidiaries, it would mean that where a conflict arises between their objectives and those of the government, their objectives would prevail, since *de facto* control resides with management which they control. This is a possible source of friction between the IOCs and the government. In the long run, control of management by the IOCs may not be to the government's overall advantage. There is the possibility, that the government may resort to nationalization if its objectives continues to be thwarted by th

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[113] Asante, *supra*, note 98 at 350.

[114] *Ibid*.

[115] *Ibid*.

IOCs through their control of management of the subsidiary oil companies.[116] Efficiency could still be maintained if *de facto* control is vested in the boards of the subsidiaries of the IOCs. There is, therefore, no correlation between inefficiency and management control by the boards of the subsidiary oil companies.

It should be pointed out in unequivocal terms that the aim of this assessment of equity participation is not to make a case against such arrangements. Although equity participation has not secured *de facto* control by the government of the oil industry, it has redefined the working relationship between the IOCs and the government.[117] It marked the beginning of a partnership arrangement between the government and the IOCs and a furtherance of one of the objectives of the government i.e. the increase of its revenue from the oil industry, although as pointed out earlier, this objective could have been secured by other means. If properly monitored, equity participation could serve as a useful mechanism for management and technical training of Nigerians.[118] In addition, equity participation could also provide access to the operational strategies, policies, and techniques of the IOCs.[119] The above assessment is meant to point out some of the pitfalls in equity participation that may effectively undermine the development strategies of the government.

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[116] See for example, the governments nationalization of British Petroleum assets in 1979. The government asserted that its nationalization of all British Petroleum assets was a move without further implications for the other oil producing companies, "*as long as they continue to respect the policies of the Nigerian government....*" (Emphasis is mine). See (1979) September Vol.XLVI No.9, The Petroleum Economist at 377.

[117] "The Multinational Oil Companies: The Impact of Changing Relationships with Host Governments" in (1978) September 4, Vol.IX, Supplement No.36 OPEC Bulletin at xii.

[118] Asante, *supra*, note 98 at 357.

It has been argued that the government can overcome these formidable difficulties by invoking its sovereign right to impose an external regime of laws, regulations and administrative practices which may substantially achieve the *de facto* control that has eluded its representatives in the boardroom.[120] An examination of the *Nigerian Enterprises Promotion Decree* of 1972 [121] may, therefore, provide valuable lessons which could be taken account of in contractual arrangements, such as equity participation.[122] Such an examination points to the reasons for the failure of this law and offers indications as to those requirements, which may enable *de facto* control to be achieved over foreign controlled companies in general and oil companies in particular.

In 1972, Nigeria enacted its first Enterprises Promotion Decree, which was intended to increase ownership by Nigerians in business enterprises. When it later became apparent that the objectives of the government could not be achieved, it appointed a commission in 1972 [123] to examine the Decree with a view to *inter alia*:[124]

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[119] *Ibid.*

[120] *Ibid.* at 358.

[121] This Decree was repealed by the 1977 Decree. The 1977 Decree has also been repealed by the *Nigerian Enterprises Promotion Decree* of 1989.

[122] Asante & Stockmayer, *supra*, note 107 at 60.

> Report on the development and use of indigenous managerial capacity in the country and on managerial structure of business affected by the scheme and foreign controlled companies in Nigeria and recommend measures which will ensure that managerial responsibilities are assigned to Nigerian executives.

In its Report, the commission held that one of the basic defects of the Decree was the "failure to match equity participation with management control by Nigerians."[125] The commission recommended several measures to correct these shortcomings. For example, it recommended that certain key posts in businesses should be reserved exclusively for Nigerians. Its first proposal was that Nigerians should be appointed to all chief executive positions in foreign controlled companies.[126] The government agreed generally with the recommendations, but was sceptical about its implementation.[127] The government believed that the fixed time schedule for an across-the-board measure of managerial replacement by Nigerians could not be fulfilled.[128]

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[123] The Industrial Enterprises Panel also known as the Adeosun Commission, referred to in Asante & Stockmayer, *ibid.* n.41.

[124] Asante & Stockmayer, *ibid.* at 60.

[125] *Ibid.* at 61. See also Kachikwu, *supra*, note 13 at 177. The author submits that: "The programme of indigenization has, ...undoubtedly failed to achieve the much sought after local controls by Nigerians."

[126] Asante & Stockmayer, *ibid.*

[127] *Ibid.* It was the report of the panel that formed the basis of the repealed 1977 Decree.

[128] Asante & Stockmayer, *ibid.*

Instead, the government preferred a piecemeal approach which required the training of Nigerians in technical and managerial skills and the obligation to employ qualified Nigerian personnel to managerial positions.

The above examination of the 1972 Decree reveals that while national management is deemed vital for an improved control matching local equity shareholding, management can only be changed by supporting measures, such as the training and employment of qualified Nigerian personnel to management position.[129] The inability of Nigeria to exercise *de facto* control over its oil industry is the result of the absence of domestic personnel for management positions in the subsidiaries of the IOCs.[130] Even if domestic personnel are available to assume managerial position, the success in the form of *de facto* control is far from being assured.[131] Nigerians appointed to top management positions in the subsidiaries of the IOCs, may take the viewpoint of their headquarters in America or Europe. This may be due to their inexperience and/or the presence of an established corporate practice.

The training of Nigerians in petroleum technology, managerial skills and the obligation to hire qualified Nigerian personnel to senior posts are two first steps, which may lead to *de facto* control by Nigerians of the oil industry.[132]

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[129] *Ibid.*

[130] Olorunfemi, *supra*, note 106 at 25-26.

[131] Asante & Stockmayer, *supra*, note 107 at 61.

[132] *Ibid.* Under Part IV, paragraph 26 of the Regulations, the licensee of an OPL shall within twelve months of the grant of his licence, and the lessee of an OML shall on the grant of his lease, submit for the Minister's approval a detailed programme for the recruitment and training of Nigerians in all phases of

These two policies, over time, would generate a pool of managers and, thus, achieve the objective of *de facto* control of the oil industry. According to Kachikwu:[133]

> In the final analysis, it would depend on the emerging Nigerian entrepreneurial class to acquire control, if they wish through skillfully developing their technological and managerial know how, understanding the rudiments of corporate control structures and mechanisms, and most important, developing a kind of entrepreneurial behaviour pattern that places greater emphasis on innovations and successful operations of businesses to attain national goals, than a steady rush to quick wealth.

Whether this will succeed will also depend on the formulation of an oil policy which is sufficiently clear and flexible to serve as guidelines for management decisions.[134] *De facto* control of the oil industry hinges upon the capacity of the government to create a comprehensive system of management control by Nigerians. Unless this is done, it remains of secondary importance whether the government acquires majority equity shares in the Nigerian subsidiaries of the IOCs.

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petroleum operations. In addition, under paragraph 29 of the Regulations, the petroleum operator has an obligation to report on the training programme and Nigerianization at or about the end of June or December each year. The Minister may revoke a licence and/or lease for failure to comply with the above provisions. See paragraph 24(1)(b) of the Act. It has been argued in section 2.2.f. above, that the effectiveness of this power of revocation is in doubt. The government should be directly involved in the training of Nigerian personnel in all phases of petroleum operations. The Petroleum Training Institute in Warri must be strengthened in order for it to be able to effectively undertake this role. In addition, the government must undertake the training of Nigerian personnel abroad.

[133] Kachikwu, *supra*, note 13 at 178.

[134] Asante & Stockmayer, *supra*, note 107 at 61.

Chapter 3

ACQUISITION OF OIL RIGHTS UNDER CONTRACTUAL JOINT VENTURES

3.0. Introduction

In the preceding chapters, we examined the different modes of acquisition of oil rights by the international oil companies (IOCs) under the repealed *Mineral Oils Ordinance* of 1914 and the changes introduced by the *Petroleum Act* of 1969. In this chapter, we shall critically inquire into the different modes of acquisition of oil rights by the IOCs under contractual joint ventures. These contractual joint ventures consist of the production sharing and service contracts.

In the first section, we briefly examine the choice of legal framework available to an oil producing country (HC) wishing to undertake the exploration and exploitation of its oil resources. Such an exercise is necessary because it provides a basis for comparison of the relative merits of acquisition of oil rights under a petroleum code, such as the *Petroleum Act* of 1969, with acquisition of oil rights under contractual joint ventures.

In sections two and three, we analyze the basic features of the production sharing and service contracts respectively. Where necessary, reference will be made to the different modes of acquisition of oil rights by the IOCs under contractual joint ventures in other countries, particularly in OPEC member states. This comparative study will, thus, enable us to assess the Nigerian production sharing and service contracts and make recommendations for their improvements.

In the concluding section of this chapter, we shall look into the problem of contractual stability in international oil contracts. By so doing, we highlight the importance of renegotiation clauses, not only as a mechanism for preventing conflict between HCs and IOCs, but also as a means which could assist HCs to achieve their objectives. Finally, we argue that the rights acquired by the IOCs under the different modes of acquisition of oil rights can be adjusted when circumstances change in the oil industry.

3.1. Choice of Legal Framework

A HC seeking to develop its oil resources must determine the structure under which it plans to foster their exploration and exploitation.[1] The development of new forms of arrangements presents HCs with a range of choice. In making its choice, a HC must:[2]

> Look beyond symbols to the specific provisions and mechanisms which make up the total package and assess how effectively these serve the interests which are to be secured.

Several structures exists for the acquisition of oil rights for the exploration and exploitation of oil resources. These are:

3.1.a. The "Fixed Content System"[3]

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[1] See K.W. Blinn, et al *International Petroleum Exploration and Exploitation Agreements - Legal, Economic, and Political Aspects* (New York: Barrows Co., Inc., 1986) at 3. [Hereinafter Blinn].

[2] K. Hossain, *Law and Policy in Petroleum Development* (London: Frances Pinter (Publishers) Ltd., 1979) at 173.

[3] Blinn, *supra*, note 1 at 34.

Under this system, the legislation fixes in advance conditions under which rights to explore for and/or exploit oil resources may be granted under standard form licences or leases.[4] The principal advantage of the "fixed content system" from the point of view of the HC is that the terms, in particular fiscal terms fixed by legislation, can be varied by subsequent legislation.[5] For example, in a study of Canadian petroleum legislation, Thompson observed that:[6]

> The oil producing jurisdictions in Canada have developed a legal mechanism for controlling oil agreements, so that the relation between the government and the oil company can be made responsive to changes which the public interest dictates. This mechanism is a clause in oil agreements requiring the oil company to accept as binding all legislative and regulatory changes which may be enacted or promulgated from time to time in the future.

It was this mechanism that enabled the province of Alberta in the early sixties to respond to changes in the environment in the oil industry by resorting to legislation to alter existing petroleum development arrangements.[7] The Alberta

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[4] Hossain, *supra*, note 2 at 100.

[5] *Ibid.* at 102. A good example of this can be seen in Nigeria where the fiscal terms originally fixed by the *Petroleum Profits Tax Act* of 1959 has constantly been amended. See *Petroleum Profits Tax Act* 1959 (as amended). Today however, the taxes payable by the IOCs are computed under the revised memorandum of understanding (MOU) between the Nigerian government and the IOCs.

[6] A.R. Thompson, "Sovereignty and Natural Resources - A Study of Canadian Petroleum Legislation" (1967) 1 Val. U.L.Rev. 284 at 290, referred to in Hossain, *ibid.* at 103.

[7] Hossain, *ibid.* at 104. This same provision is currently in use in Alberta. For example, a standard petroleum and natural gas lease or licence granted by the government contains the following provisions:(1)In this licence, a reference to the Mines and Minerals Act or to any Act of the legislature of Alberta....shall be construed as a reference to (a) that Act, as amended from time to time,(b) any replacement of all or part of that Act from time to time enacted by the legislature, as amended from time to time, and (c) any regulations, orders, directives....from time to time made under any enactment referred to in....(a) or (b), as amended from time to

Mines and Minerals Act was amended in 1962. The term of renewal of existing leases were changed to ten (10) years in place of twenty one (21) years and drilling commitments were to be enforced over five (5) years instead of one (1) year.[8]

In addition, the "fixed content system" would seem to have the advantage of giving assurance of equal treatment to all licensees or lessees and, therefore, give the impression that the terms are not negotiable.[9] This would give the HC a stronger hand when discussing the terms or conditions with the IOC.[10] However, the rigidity of the "fixed content system" may make it difficult to attract IOCs to an exploratory programme. This is because the lack of flexibility may lead to a situation where standards may be set which are too high or are set too low and, thus, defeat some of the important objectives and

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time (*Change of law clause*); and (2) the licensee or lessee shall comply with the provision of (a) the Mines and Minerals Act, and (b) any other Acts of the legislature of Alberta that affect the rights and obligations of the licensee or lessee of petroleum and natural gas (*Compliance with law clause*). In Nigeria, a provision to the same effect can be found in the various forms of contractual arrangements, e.g. *clause* 15 of the production sharing contract between the Nigerian National Petroleum Corporation (NNPC) and Ashland Oil (Nigeria) Company (AON), which provides that: "No term or provision of this contract....shall prevent or limit the government of Nigeria from exercising its inalienable rights."

[8] Hossain, *ibid*. See also the Nigerian *Petroleum Act* of 1969 which repealed the *Mineral Oils Ordinance* of 1914 and reduced the term of oil mining leases from 30 years (onshore) and 40 years (offshore) to 20 years. Oil mining leases granted prior to 1969 were however not affected. See section 2.2.g. of chapter 2.

[9] Blinn, *supra*, note 1 at 34.

[10] *Ibid*. See also Hossain, *supra*, note 2 at 107.

interests of the HC.[11] Also, as Alberta shows, the "fixed content system" is not really fixed, and may, therefore, create the risk that the IOCs will be bound to more adverse terms in the future.

3.1.b. The "Agreement System" [12]

Under this system, there is no legislative authorisation, or the legislation is of a very general nature, and it is left to the government, through its state-owned oil company, to grant rights to explore for and/or to exploit oil resources on the basis of individually negotiated agreements.[13] Although these individually negotiated agreements may provide the maximum degree of flexibility to the HC during the negotiation stage, it may prove difficult for the HC to change the terms and conditions stipulated in the agreement after it has been signed.[14]

3.1.c. The "Flexible System" (or Hybrid System)[15]

Under this system, the legislation lays down general guidelines and conditions which must be satisfied by applicants seeking to acquire exploration rights, but provides for certain important terms and conditions to be settled by negotiation.[16] It is evident that the "flexible system", which combines elements of both the "fixed content system" and the "agreement system", is increasingly being used by several countries.[17] This does not mean, however, that a "fixed content system" under a legislation will not yield results as good as those that occur under the "flexible system." On the contrary, in countries with a strong and efficient institutional framework, backed by clear and carefully devised objectives and strategy, the distinction between the two systems might be negligible.[18] This is because a country with a "fixed content system" may have well-defined objectives set out in its energy policy, which enables it to maintain a degree of flexibility in negotiating oil agreements with the IOCs.

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[11] Blinn, *ibid.* and Hossain, *ibid.* See also S.K. Date-Bah & M. Rahim, "Promoting Petroleum Exploration and Development: Issues for Government Action" in K. Khan ed., *Petroleum Resources and Development - Economic, Legal and Policy Issues for Developing Countries* (London: Belhaven Press, 1987), 93 at 95.

[12] Blinn, *ibid.*

[13] Hossain, *supra,* note 2 at 101.

[14] Blinn, *supra,* note 1 at 34. In Nigeria, however, as a result of the good relationship between the government and the IOCs, contractual flexibility has been achieved through the process of renegotiation. See memorandum of understanding (MOU) and OPEC Declaratory Statement of Policy of 1968 (Resolution XVI.90), *infra,* notes 46 & 149.

[15] Blinn, *ibid.*

In Nigeria, although the *Petroleum Act* of 1969 falls within the framework of the "flexible system", there are other types of contractual arrangements under which oil rights could be acquired by the IOCs for oil exploration and production. Although similarly involving NNPC's participation in some forms, they do not result in the grant by NNPC of oil exploration licences, oil prospecting licences or oil mining leases.[19] These other forms of arrangements for the acquisition of oil rights by the IOCs, fall within the framework of the "agreement system." They are the production sharing and service contracts.

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[16] Hossain, *supra*, note 2 at 101. The repealed *Mineral Oils Ordinance* of 1914 fell within the framework of the flexible system.

[17] Blinn, *supra*, note 1 at 34 and Date-Bah & Rahim, *supra*, note 11 at 96.

[18] Date-Bah & Rahim, *ibid*.

[19] G. Etikerentse, *Nigerian Petroleum Law* (London: Macmillan, 1985) at 42.

As mentioned in chapter 1, in 1972, the federal government of Nigeria reserved all rights to explore for and produce mineral oils and natural gas in Nigerian territory for the NNPC with the exception of those areas in which there were subsisting grants of petroleum rights. The areas reserved included areas subsequently surrendered, relinquished or forfeited to the government. The NNPC (formally known as the Nigerian National Oil Corporation) under section 3 of the *Nigerian National Oil Corporation Decree* 1971, is authorized to "enter into contracts or partnerships with any company, firm or person which in the opinion of the corporation will facilitate the discharge of its duties under this Decree." Consequently, the NNPC has the right, power and authority to enter into contractual joint ventures with the IOCs in respect of areas not covered by existing oil rights. In furtherance of this power, the NNPC has entered into several contractual joint ventures with the IOCs. These contractual joint ventures are the modern modes by which oil rights could be acquired by the IOCs. Unlike the oil exploration licences, oil prospecting licences and oil mining leases which could be obtained by an application to the Minister of Petroleum Resources,[20] the production sharing and service contracts are open to public bidding when announced by the NNPC. In sections two and three, we shall discuss the basic features of these contractual joint ventures.

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[20] See section 2.2. of chapter 2.

3.2. Contractual Joint Ventures

It was the quest for control and increased financial returns on the part of HCs, that gave rise to new varieties of contractual arrangements under which oil rights could be acquired by the IOCs.[21] These arrangements represent a substantial departure from the framework of acquisition of oil rights under the *Petroleum Act* of 1969. The common feature of these new forms of contractual arrangement is that they affirm the status of the HC as the "undisputed owner of the natural resources to be developed."[22] However, according to Asante:[23]

> Notwithstanding the undoubted political significance of ownership, some commentators have suggested that the functional implications of the new forms of contractual arrangements are not markedly different from those of a concession.

The truth of this assertion can only be determined after an examination and assessment of these new forms of contractual arrangements by which oil rights could be acquired by the IOCs and it is to this that we now turn.

3.2.a. The Production Sharing Contract (PSC)

The PSC represents one of the modes by which an IOC can, through

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[21] S.K.B. Asante, "Restructuring Transnational Mineral Agreements" (1979) 73 American J.I.L. 335 at 359. See also R.F. Mikesell, *Petroleum Company Operations and Agreements in the Developing Countries* (Washington, D.C.: Resources for the Future, Inc., 1984) at 25, where the the author submits that these new forms of contractual arrangements are the result of strong political antagonism towards IOCs brought about by the new ideology of permanent sovereignty over natural resources.

[22] Asante, *ibid*.

[23] *Ibid*. at 360.

agreement, acquire oil rights for exploration and production of oil. This form of contract, which was first pioneered in Indonesia in 1967, is a relatively new legal instrument for defining the relationship between HCs and IOCs.[24] This contractual structure, while it has evolved to take into account the particular circumstances of the venture concerned and to keep pace with the development of relationships between HCs and IOCs, has nevertheless retained its basic features.[25] These features include:[26]

(i) The IOC is appointed by the HC as contractor on a certain area;

(ii) the IOC operates at its sole risk and expense under the control of the HC;

(iii) the production, if any, belongs to the HC;

(iv) the IOC is entitled to a recovery of its operating costs out of the production from the contract area (referred to as "cost oil");

(v) after recovering its operating cost i.e. "cost oil", the balance of production (referred to as "profit oil") is shared on a pre-determined percentage split between the HC and the IOC;

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[24] Blinn, *supra*, note 1 at 69. A production sharing contract bears some resemblance to a farmout arrangement. In a typical farmout arrangement, a lessee contracts to transfer acreage to a company if the company drills a well. Once payout occurs and the driller recovers all the costs of drilling the well, the driller and the lessee share the proceeds of production on a predetermined formula. See E.E. Smith & J.S. Dzienkowski, "A Fifty - Year Perspective on World Petroleum Arrangements" (1989) 24 Texas I.L.J. 13 at 37 n.174. For a study of Canadian farmout agreements see A.R. Lucas & C.D. Hunt, *Oil and Gas Law in Canada* (Toronto: Carswell, 1990) at 145-161.

[25] Blinn, *ibid*. See also K. Khan, "Petroleum Taxation and Contracts in the Third World - A Law and Policy Perspective" (1988) 22 J.W.T.L. 67 at 83-84 and Mikesell, *supra*, note 21 at 28.

[26] Blinn, *ibid*. at 69-70.

(vi) the IOC's income is liable to taxation; and

(vii) the equipment and installations are the property of the HC, either at the outset or progressively in accordance with the amortization schedules.

The Nigerian PSC differs in certain respect from the standard PSC which was pioneered in Indonesia. Its basic features will be considered in the following section.

3.2.b. The Nigerian Production Sharing Contract (PSC)

Presently, the only example of a PSC in Nigeria is the one between the Nigerian National Petroleum Corporation (NNPC) and Ashland Oil (Nigeria) Company (AON), the Nigerian subsidiary of an American company.[27] Although the contract was signed on the 12th of June 1973, its effective date was 1979 and it extends for a duration of twenty years. No explanation was given as to why the effective date was 1979 instead of 1973, the date the contract was signed. The principle features of the NNPC-AON production sharing contract include the following:

3.2.b.i. Rights and Obligations of AON under the PSC

The position of AON under the NNPC-AON production sharing contract is defined by a set of obligations and rights which are included in the PSC. The most important of these are:

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[27] See *Basic Oil Laws and Concession Contracts South and Central Africa, (Original Texts), Supplement* Nos. 51-55 (1978-1979).

(a) Operating Costs

Clause 1 provides that AON shall bear the risk of operating costs required in carrying out petroleum operations in the contract area. This clause, thus, imposes an obligation on AON to furnish the entire money for the costs involved in exploration, drilling, production and the day-to-day operation of the PSC joint venture.[28] In addition, AON is required to provide the technical expertise for the performance of the work programme.[29]

(b) Reimbursement of AON's Operating Costs and Sharing of Profits

The reimbursement of AON's costs incurred on behalf of the joint venture operations is dependent on the production of petroleum in commercial quantity which will be sufficient to compensate AON for its operating costs.[30] The operating cost recoverable by AON out of the available oil is known as "cost oil." Under clause 6 of the PSC, AON is entitled to recover not only its operating costs but also interest costs on funds borrowed to conduct petroleum operations. This is fixed up to a maximum of forty per cent (40%) per annum of available crude oil. Any unrecovered operating costs from previous years are carried forward until fully recovered by AON.

Fifty five per cent (55%) of the remaining sixty per cent (60%) after allocation of "cost oil" to AON, shall be allocated to AON and the net realized price received for such "tax oil" shall be applied by AON towards payment of petroleum profit tax payable for the production. The balance of the available production after the allocation made for "cost oil" and "tax oil" is termed "profit oil." Of this "profit oil", NNPC shall be entitled to take and receive sixty five per cent (65%) and AON shall be entitled to take and receive thirty five per cent (35%); provided however, that when daily production of available crude oil from the contract area exceeds fifty thousand (50,000) barrels per day, the participating interests which shall apply shall be NNPC seventy per cent (70%) and AON thirty per cent (30%) of the five per cent (5%) "profit oil."

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[28] Etikerentse, *supra*, note 19 at 42.

[29] *Ibid.*

[30] *Ibid.* Under Clause 1(g), commercial quantity is defined as "the capacity to produce at least 10,000 barrels per day of crude oil from the contract area."

This cost recovery provision, which is also a feature of the standard PSC, is particularly attractive to the IOCs. It enables the IOCs to obtain a quick pay-out of forty per cent (40%) of the oil towards reimbursement of exploration, development and other operating costs they have incurred.[31] On the other hand, a HC might regard the forty per cent (40%) cost recovery as excessive. For example, in response to the 1973 oil price increase, Indonesia sought alteration in the contractual terms with the IOCs, so that the existing cost recovery allowance of forty per cent (40%) would be reduced to twenty five per cent (25%), and the ratio in which the remaining production would be shared between the government and the company would be altered from 60%/40% to 85%/15%.[32] The IOCs reacted adversely to this change and undertook hardly any new exploration, until the proposed amendments were substantially modified.[33]

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[31] Hossain, *supra*, note 2 at 148.

[32] *Ibid*. at 104.

(c) Payment of Taxes

The first PSC negotiated in Indonesia did not provide for the payment of income tax by IOCs.[34] However, this has changed and IOCs operating in Indonesia are liable to a forty five per cent (45%) tax on their income arising from operations.[35] Under the NNPC-AON production sharing contract, petroleum profit tax of fifty five per cent (55%) is paid from the available crude oil after the deduction of AON's "cost oil." This is referred to as "tax oil." The "tax oil" is made up of the tax payable by the NNPC and AON. This is allocated to AON and the price realized after the sale of "tax oil" shall be applied by AON towards the payment of petroleum profit tax payable for the production. Any additional amounts of petroleum profit tax due after application of the fifty five per cent (55%) for "tax oil", shall be paid by NNPC and AON in proportion to their participating interest shares at the time such additional amount of petroleum profit tax is payable. It has been observed that for administrative convenience AON in practice also pays, on behalf of NNPC, the taxes and royalties payable by NNPC in respect of NNPC's share of the joint venture production.[36]

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[33] *Ibid.* at 149.

[34] Blinn, *supra*, note 1 at 77.

[35] *Ibid.* See section 3.2.b.i.(b) above on the percentage split between the Indonesian government and the IOCs under a PSC.

In Libya, income tax is not imposed under a PSC, but the share of production retained by the national oil company (NOC) is as high as eighty one per cent (81%) against nineteen per cent (19%) for the IOC.[37] There is however, no practical significance whether the tax is included in the HC's share of "profit oil" or paid by the IOC.[38] The mechanism adopted depends on its political and administrative convenience for the HC.[39]

(d) Control and Management of Operations

The management provisions in the Indonesian PSC were regarded in the late sixties, when it was first introduced, as "a radical departure from conventional arrangements existing in other parts of the world, for it asserted that Pertamina (the national oil company) shall have and be responsible for the management of the operations contemplated", while the contractor would be responsible to Pertamina "for the execution of such operations."[40]

This provision is absent in the NNPC-AON production sharing contract. It appears, therefore, that the ultimate responsibility of control and management of petroleum operations is vested with AON. Although such a management clause has never been enforced under most PSCs, since it is difficult, in practice, to separate the overall management of operations from their day-to-day conduct, especially where only one party (the IOC) bears the financial risk of operations,[41] its absence from the NNPC-AON production sharing contract calls into question the government's objective of ultimately securing the overall control and management of the oil industry.

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[36] Etikerentse, *supra*, note 19 at 43.

[37] Blinn, *supra*, note 1 at 77.

[38] *Ibid*.

[39] *Ibid*.

[40] *Ibid*. at 78. See also Hossain, *supra*, note 2 at 140.

(e) Work Programme and Expenditure

Under clause 4 of the NNPC-AON production sharing contract, AON shall within three months after the effective date (subject to any necessary extensions granted by NNPC), commence seismic investigations in the contract area and thereafter shall commence drilling operations in accordance with sound international petroleum exploration practice. In addition, if geological conditions warrant, AON shall commence drilling operations not later than eighteen months after the effective date of the contract. AON shall also within one month after the effective date and thereafter at least two months prior to the beginning of each year prepare and submit for approval to NNPC, which approval will not be unreasonably withheld, a work programme and budget for the contract area. Any revision of the work programme and budget proposed by NNPC must be done within thirty days after receipt thereof. If NNPC fails to advise AON of any revision to the work programme and budget, it shall be deemed to be approved.

In relation to expenditure, clause 4 also provides that the amount to be spent by AON in conducting petroleum operations in the contract area during the first two years, shall in the aggregate be not less than the equivalent of five million, five hundred thousand United States dollars (U.S.$5,500,000). Such amount to be prudently expended by AON with the concurrence of NNPC. It would, however, be very difficult for the NNPC to monitor the costs being incurred because the level of expenditure might be affected by inflation.[42]

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[41] Blinn, *ibid.* and Hossain, *ibid.*

(f) Marketing of Available Oil

Under clause 6 of the NNPC-AON production sharing contract, AON has the right to sell on behalf of the joint venture the quantity of the available production made up of:[43]

(a) "Cost oil."
(b) "Tax oil."
(c) AON's "participating interest."
(d) NNPC's "participating interest." (on request by NNPC).

Control over marketing acquires importance in relation to pricing and the price of oil is relevant for the computation of the government's share of profits and other dues.[44] If the price of oil in the world oil market drops, the realized price from the sale will also drop and the government's share from "profit oil" as well as taxes and other dues payable to the government will decrease.[45] In addition, there will be no incentive on the part of the IOCs to carry out any further exploration activities. This is because whenever the price that the IOCs obtained from the market was lower than the official selling price, the companies were taxed on the official selling price. This meant that the IOCs paid more tax than would have been due had the computation of tax been based on the actual market price and not on the official selling price. This reduced their profit margin. It was this unhealthy situation that led to the memorandum of understanding (MOU) between the Nigerian government and the IOCs.[46]

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[42] Hossain, *ibid.* at 141.

[43] Etikerentse, *supra*, note 19 at 43.

[44] Hossain, *supra*, note 2 at 117.

[45] *Ibid.*

Under clause 7, if a more favourable *bona fide* price is available to NNPC than to AON for the amount of "cost oil" or "tax oil", NNPC shall advise AON in writing and, within ten days after the receipt of such advice from NNPC, AON shall notify NNPC regarding AON's intention to meet the more favourable price. In the absence of such notice from AON, NNPC shall market the said amounts of "cost oil" or "tax oil."

(g) Training of Nigerians

Under clause 5(1)(h), AON is required in implementation of work programmes and in accordance with the contract to prepare and carry out plans and programmes for industrial training and education of Nigerians for all job classifications with respect to petroleum operations in accordance with the *Petroleum Act* 1969. In addition, under clause 12, AON shall within two months after the effective date and after consultation with NNPC submit a detailed programme for recruitment, and within four months submit a training programme for Nigerians in the conduct of all petroleum operations.

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[46] The 1986 MOU came into effect on 1st January 1986 and was amended in May 1991. It fixed a notional price (generally referred to as "posted" prices) as the basis for realisation of taxes and other dues payable to the government. The MOU therefore acts as an insurance against low profits and additional chargeable tax does not occur under the MOU. See Mikesell, *supra*, note 21 at 26-27 and also Petroleum Taxation Legislation Report No. 138, September/October 1991 at 52.

The main objective of these provisions concerning manpower training is to enable Nigerians to control and operate all phases of the oil industry. However, this obligation has not been vigorously pursued by the NNPC and the IOCs. The training of Nigerians in petroleum technology is one of the most complex issue confronting the country. Since the IOCs are the principal agents for conveying petroleum technology, the question has arisen as to whether Nigeria should rely exclusively on the IOCs for the training of Nigerians in petroleum technology or whether it should make efforts, devise programmes and create arrangements which would lead to the development or acquisition of petroleum technology.[47] There is no doubt that if the objective of the Nigerian government in exercising *de facto* control of the oil industry is to be achieved, the government must be involved in the training of Nigerians in petroleum technology. Another reason for the lack of success in the training of Nigerians in petroleum technology can be traced to the sophisticated and capital-intensive nature of petroleum technology, which becomes obsolete so quickly, because of the fast changing nature of the industry and the need to find new ideas to deal with these changes.[48]

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[47] K. Khan, "The Transfer of Technology and Petroleum Development in Developing Countries: With Special Reference to Trinidad and Tobago" (1986) 4 No. 1 J.E.N.R.L. 10 at 10.

It must now be recognized that the ability to develop or acquire petroleum technology does not lie solely with the IOCs. Petroleum technology can only be developed or acquired through the process of training and adequate exposure to it. These provisions on the training of Nigerians in petroleum technology will have little effect no matter how stringently they are worded.[49] The primary objective which would prove beneficial in the long run is the development or acquisition of petroleum technology. Permanent sovereignty over its oil resources can only be attained by the Nigerian government through the development or acquisition of petroleum technology so as to be able to control operations in the petroleum industry directly.[50] A country that cannot boast of having the technology necessary for running its oil industry can hardly lay claim to permanent sovereignty over its oil resources.

It is also worrisome to note that Nigeria, with a daily average production of 2 million barrels of oil per day has no energy policy.[51] This has contributed to the lack of technological capability to run its oil industry. Any reform must, therefore, start with the formulation of a national energy policy.[52] Such a policy should provide for:

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[48] O.A. Alegimenlen, "Issues in the Acquisition of Petroleum Development Technology for Third World States" OPEC Review Vol. XV, No.2 Summer 1991, 123 at 123.

[49] Y. Omorogbe, "The Legal Framework for the Production of Petroleum in Nigeria" (1987) 5 No. 4 J.E.N.R.L. 273 at 288.

[50] *Ibid.* at 287-288.

[51] The average daily production for the year 1990 totalled 1.83 million barrels of oil as distinct from the OPEC quota of 1.61 million barrels of oil. Source: National press briefing by the Minister of Petroleum Resources on the activities of his Ministry for the year 1990, published in The Guardian Newspaper, May 1, 1991. In the second quarter of 1992 the daily productive capacity rose to 2 million barrels of oil. See (1992) June 1-7 West Africa Magazine at 927.

(i) The training of Nigerian personnel in the various aspects of petroleum technology;[53] and

(ii) the "Simple rationalization or scientific management" using the skills acquired in (i) above.[54] This would involve the "rearrangement of prior knowledge" (i.e. adopting known ideas or methods in new combinations).[55]

It is this "rearrangement of prior knowledge" that would eventually lead to the development or acquisition of petroleum technology. This process of technological innovation involves borrowing, adapting and experimenting with ideas already present in our fund of scientific knowledge.[56]

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[52] A. Adams, "Setting the Ground-rules for a Viable National Energy Policy" (1988) December/January OPEC Bulletin at 6.

[53] Khan, *supra*, note 47 at 22.

[54] M. De Chazeau and A.E. Kahn, *Integration and Competition in the petroleum Industry, Petroleum Monograph Series*, Vol. 3 (New Haven: Yale University Press, 1959) at 281.

[55] D.H.N. Alleyne, "State Petroleum Enterprises and the Transfer of Technology" in United Nations ed., *State Petroleum Enterprises in Developing Countries* (New York: Pergamon Press, 1980) at 112.

[56] *Ibid.*

Recently, the Minister of Petroleum resources in his press briefing said:[57]

> The ministry, in consultation with appropriate agencies in the petroleum sector of the economy, has produced a draft policy for the industry....The objective is to develop immediate and long term policies and pursue programmes that will enable our oil industry survive and compete internationally.

On training, he said:

> The ministry will continue to place emphasis on the training and re-training of its officers so that they will be in a position to meet the challenges of the highly dynamic industry. Towards this end, officials of my ministry are working on a comprehensive training policy....In the area of manpower development and technology transfer my ministry is initiating action on the review of the petroleum technology development fund (PTDF), which was established in 1973, by Decree No. 25 to accelerate the training of Nigerians in petroleum technology.

While this statement addresses the issue of training, it makes no reference to the issue of "Simple rationalization or scientific management" referred to in (ii) above.

It is of fundamental importance that Nigeria assumes the responsibility for its own technological advancement and should not solely rely on the IOCs for the training of Nigerians in petroleum technology. A national energy policy that fails to address this issue is not likely to succeed. In comparison with other oil producing developing countries, Nigeria is lagging behind. Although state participation in the oil industry has been achieved, the management and technical knowledge is still controlled by the IOCs. In Algeria, the "joint venture - project on line" approach which allows the state oil company to take an active part in its petroleum industry has led to the acquisition of petroleum technology.[58] The country can now boast of an exportable petroleum capability and a domestic expertise in the industry. The Algerian state oil company (SONATRACH) now effectively controls its oil industry. Similarly, Brazil, Venezuela, and Indonesia have achieved successes in the acquisition of petroleum technology.[59]

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[57] *supra*, note 51. See also M. Kassim-Momodu, "Petroleum - New Government policy" (1990) 8 No. 2. J.E.N.R.L. 149. The Petroleum Training Institute in Warri, Nigeria, provides for the training of Nigerians in the basics of Petroleum technology.

It is, therefore, suggested that the NNPC should enter into bilateral co-operation and technical assistance agreements with these countries.[60] The NNPC needs foreign assistance from these countries, which "can act as a catalyst to initiate and establish a base for research and training activities."[61] Unless there is an articulated energy policy along these lines, Nigeria would continue to depend on the IOCs for the technology required for the development of its petroleum industry.

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[58] Khan, *supra*, note 47 at 23.

[59] Omorogbe, *supra*, note 49 at 287-288.

[60] Khan, *supra*, note 47 at 23. In 1989 the organisation of African Petroleum Producers Association was formed (APPA). Its main objective is to further mutual assistance and cooperation among member nations in all aspect of the petroleum industry.

[61] It has also been suggested, that state petroleum corporations should set aside part of their earnings for research, training and development of their industry. See Khan, *ibid*. In Nigeria, see the petroleum technology development fund (PTDF) set up by *Decree No.25* of 1973.

3.2.b.ii. An Assessment

The PSCs are the result of efforts by HCs to modify the modes of acquisition of oil rights by the IOCs and, above all, to find an alternative to the traditional concession agreement which would enable the HC to exercise more control over both petroleum operations and the ownership of production.[62] It is important to point out that in assessing the PSC, as well as other forms of contractual arrangements, under which oil rights may be acquired by the IOCs, one must look behind the forms and labels.[63] The modern day PSC may not be at any higher scale of evolution than the traditional concession.[64] The structure of the agreement must be assessed and it success depends on whether it secures the interests and objectives of the HC.[65] Among the general objectives which a HC seeks to secure, the principal ones are maximisation of government revenue, control over operations, and development of national capabilities in the field of petroleum operations, so as not only to be able effectively to monitor operations, but also ultimately to undertake those operations directly.[66]

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[62] Blinn, *supra*, note 1 at 79.

[63] Hossain, *supra*, note 2 at 109. See also J.E. Attwell, "Changing Relationship between Host Countries and International Petroleum Companies" (1979-1980) 17 Houston L.R. 1015 at 1015, where the writer submits that: "One must look at the substance of each agreement to determine the bottom-line financial benefits as well as the controls that are involved in the particular contractual arrangement chosen."

[64] Hossain, *ibid*. See also Mikesell, *supra*, note 21 at 136, where the writer argues that: "Model contracts employed by governments have frequently been formulated with a view of satisfying domestic ideological objections to foreign investment in petroleum production."

[65] Hossain, *ibid*.

Although the conferral of ownership of petroleum and management responsibility on the HC's national oil company is a marked departure from the management arrangements under the traditional concessions,[67] a HC may be divested of effective powers of control through transferring extensive powers of management to the IOCs.[68] In such a situation, the retention of ownership by the HC can be regarded as symbolic.[69] Similarly, the effectiveness of these provisions relating to control and management may be undermined by the HC's lack of managerial and technical skills.[70]

The NNPC-AON production sharing contract follows the Indonesian model in respect of such basic provisions as the fiscal regime, work obligations, etc.[71] It has however, been described as "less ambitious, some would say less pretentious", than the Indonesian PSC in terms of management and control.[72] The NNPC-AON production sharing contract departs from the Indonesian PSC in entrusting management and operational responsibilities exclusively to AON.

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[66] *Ibid.* at 111-112.

[67] Asante, *supra*, note 21 at 364. As noted earlier in section 3.2.b.i.(d) above, under the NNPC-AON PSC, management and control of petroleum operations is undertaken by AON.

[68] Hossain, *supra*, note 2 at 111.

[69] *Ibid.*

[70] Asante, *supra*, note 21 at 366.

[71] *Ibid.*

[72] *Ibid.*

In functional terms this distinction may be less pronounced, but it may grant to the HC's national oil company a greater leverage in insisting on a close inspection of all aspects of the operations of the IOCs, particularly the access to documents, reports, and data which would not have been possible under the usual reporting requirement.[73] The NNPC-AON production sharing contract also departs from the Indonesian PSC in providing that "title to available crude oil allocated to each party should pass at the wellhead."[74] Although this stipulation can be identified with the traditional concession regime, "technical stipulations regarding the passing of title have little or no economic or functional significance."[75] This is because the IOCs continue to exercise *de facto* control of the oil industry whether title to available crude oil passes at the wellhead or at the point of exportation.

The PSC between NNPC-AON has also come under mounting criticism from the Report of the Crude Oil Sales Tribunal.[76] The Tribunal was set up to probe the allegation of 2.8 billion naira missing from the accounts of the NNPC.

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[73] *Ibid*. Under clause 14 of the NNPC-AON production sharing contract, NNPC's officials are entitled to have access to account books kept by AON. There is however, no provision granting NNPC the right to have access to other documents, reports and data kept by AON.

[74] *Supra*, note 27, clause 6(iv).

[75] Asante, *supra*, note 21 at 366.

[76] See also F. Sasegbon, "Current Development in Oil and Gas Law: Nigeria-With Comparative Analysis with other African Oil Producing Countries" (1981) 1 Energy Law 361 at 371. The writer submits that: "After the operating company took its forty per cent (40%) of the proceeds for the amortisation of its investment and operating expenses....and after setting aside the fifty five per cent (55%) for the payment of....petroleum profit tax, the balance left was hardly anything to warrant the application of any ratio whether 35%/65% or 30%/70%".

The Tribunal in its report found no sum missing, but said:[77]

> The PSC certainly has no benefits whatsoever to the NNPC as it stands today,...it seem too lopsided in favour of Ashland....Ashland has taken the NNPC and this country for a good ride in the implementation of this contract.

The Tribunal concluded that the NNPC can, therefore, ill afford to continue this contract a day longer.[78] It appears that the Tribunal was influenced in its criticism by the percentages of available crude oil set aside for "cost oil" and tax oil", which are one of the highest seen in the oil industry. Although the percentages of available crude oil set aside for "cost oil" and "tax oil" are high, this does not justify the Tribunal's criticism. Even if the percentages of available crude oil set aside for "cost oil" and "tax oil" were to be reduced, there would be no guarantee of *de facto* government control of the oil industry.

Despite the above shortcomings of the PSCs, the IOCs prefer them, because they control their own share of the crude oil and, barring an election by the state oil company to take its share in kind, they control the destination of the HC's share of oil.[79] In addition, the IOCs have been able to enjoy price increases in the world oil market under the PSC.[80] From the HC's point of view, this is the main weakness of the PSC.

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[77] Report of the Tribunal of Inquiry into Crude Oil Sales (1980) at 25, referred to in Sasegbon, *ibid.* at 377 n.26.

[78] *Ibid.* at 371. See also Y. Omorogbe, "Contractual Forms in the Oil Industry: The Nigerian Experience with Production Sharing Contracts" (1986) 20 J.W.T.L. 342 at 345, the author submits that the PSC has the following drawbacks:"(i) The percentage of petroleum set aside per cost recovery is one of the highest seen; (ii)the imposition of petroleum profit tax is unusual, and makes this PSC the one with the highest tax rate and allied to this is the fact that a percentage of production is set aside towards the payment of tax;(iii) the contractor, realizing that it is more beneficial can concentrate on producing one lucrative field, while slowing down exploration on other areas covered by the PSC; (iv)the contractor, since its expenses will be fully met, can afford to be wasteful or extravagant to the disadvantage of the HC; and (v)the contractor may earn windfall profits when there is a great increase in the price of crude oil."

[79] Hossain, *supra*, note 2 at 157.

Recent developments have, however, shown that the PSC can be improved by incorporating into it specific provisions to safeguard different interests which are inadequately secured in a standard PSC.[81] For example, the "windfall profits" which the IOC may obtain as a result of price increases have been eliminated in Angola by the inclusion of "price cap" clauses which retain for the state any excess profit that may arise when an increase in crude oil prices exceeds the rate of increase in company cost.[82] The problem of slow exploration by the IOC under a PSC could also be eliminated if the relinquishment clause, which, for example, in Nigeria is presently fifty per cent (50%) of the contract area after ten years (10 years), is reduced to fifty per cent (50%) of the contract area after five years. This will speed up the exploration activities of the IOCs.[83] Whether this will be acceptable to the IOCs is debatable. "It seems however that the problem lies not so much in the group of contracts known as PSCs, but in the variant which is presently in force in Nigeria."[84]

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[80] *Ibid*. See also Omorogbe, *supra*, note 78 at 371.

[81] Hossain, *ibid*. at 158. See also Omorogbe, *ibid*. at 347.

[82] Omorogbe, *ibid*. In Nigeria, if there is a sharp increase or decrease in oil price, the contract can be renegotiated with the IOCs. For an example, see the MOU, *supra*, note 46 and also OPEC Declaration, *infra*, note 149.

[83] Omorogbe, *ibid*.

If the veil is lifted, it becomes evident that although the PSC may have secured for the government its objective of maximising its revenue from the oil industry, in terms of achieving the government's objectives of *de facto* control of the oil industry and the development of national capabilities in the field of petroleum operations, it has failed. In the absence of *de facto* control of the oil industry by Nigerians, the compatibility of the PSC with the principle of permanent sovereignty over natural resources is highly in doubt. It is, therefore, misleading to conclude that the evolution of oil agreements from the traditional

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[84] Y. Omorogbe, *supra*, note 49 at 281. The Model PSC of September 1990, issued by the NNPC differs from the NNPC-AON PSC. In respect of the recovery of operation cost and sharing of profit, it provides that the "cost oil" recoverable by the IOC shall be thirty per cent (30%), "tax oil" is fixed at forty per cent (40%) and the balance of thirty per cent (30%) shall be shared thirty five per cent (35%) NNPC, sixty five per cent (65%) IOC. Taxes due on the IOC's share of sixty five per cent (65%) shall be paid by the IOC in accordance with the Companies Income Tax Act, and shall not under any circumstances be reimbursable to the IOC. This provision differs from clause 6 of the NNPC-AON PSC which has been the subject of criticisms. See *Basic Oil Laws and Concession Contracts South & Central Africa (Original Text), Supplement* Nos.100-105 (1990-1991). In March 1991, the Nigerian government produced a confidential Model PSC. The 1991 Model has some substantial differences from the 1990 Model PSC. The major changes are in respect of the recovery of operating cost and crude oil allocation. *Article* 8(i) provides: (a) Tax oil; to offset actual tax and royalty due, will be deducted in full in the relevant year. Government Agency shall take in kind, lift and dispose of tax oil and from the proceed pay royalty, petroleum profit tax and concession rentals. (b) Cost oil; for cost recovery purposes, operating cost will be recovered in the year of expenditure, while capital cost will be recovered in a minimum of 20 quarterly instalments. Contractor shall take in kind, lift and dispose of cost oil and from the proceeds pay all operating cost. (c)Profit oil; crude oil after deduction of royalty, petroleum profit tax, concession rental and cost recovery. Profit oil for the Niger Delta area in the south of Nigeria, will be shared between the parties as follows:

Production level	*Percentage split: Government Agency/Contractor*
0 - 30,000 BOPD	60/40
Next 20,000 BOPD	62/38
Over 50,000 BOPD	65/35

The percentage split for offshore and frontier areas are different. See *Basic Oil Laws and Concession Contracts, South and Central Africa, (Original Text), Supplement* No. 107, 1991.

concession regime of the repealed *Mineral Oils Ordinance* of 1914 to PSC has led to the attainment by the government of its objectives. The problems of *de facto* control and national development, which persisted under the traditional concessions, can still be identified with the PSC.

3.2.c. The Service Contracts (SCs)

The IOCs can also acquire oil rights by entering into SCs with the HC. The SCs first came into existence in the late 1960s between HCs and IOCs desiring to gain access to relatively assured supplies of crude oil.[85] It is only recently that these contractual arrangements have gained currency in the wake of the development of the so-called "Brazilian Risk - Service Contract."[86] Under a service contract, the HC hires the services of an IOC, which assumes the legal status of a "contractor."[87] Thus, the contractor is not a concession holder or partner, but merely a hired agent. Service contracts are similar to PSCs. The main difference lies in the mechanism for the recovery of costs and the remuneration of the contractor.[88] Its main features include:[89]

(i) The national oil company is the sole owner of the petroleum discovered and the role of the IOC is limited to making available its financial and technological resources;

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[85] Blinn, *supra*, note 1 at 82.

[86] *Ibid*. On Brazilian Risk-Service Contract see J.S.C. Neto, "Risk-Bearing Service Contracts in Brazil" (1985) 3 J.E.N.R.L. 114.

[87] *Ibid.* See also Khan, *supra*, note 25 at 84-85.

[88] Asante, *supra*, note 21 at 360, Sasegbon, *supra*, note 76 at 371 and K. Adeniji, "State Participation in the Nigerian Oil Industry" (1977) 11 J.W.T.L. 156 at 170.

[89] Blinn, *supra*, note 1 at 88-90.

(ii) all risks and investments are placed on the IOC, which provides the capital for exploration and exploitation. This means that, unless oil is found in commercial quantities, the IOC will not be reimbursed for the expenses it has incurred in its unsuccessful search for oil;

(iii) upon the completion of the development phase (i.e. the beginning of commercial production), the HC's national oil company is authorized to take over the operations;

(iv) the amounts provided by the IOC for exploration and exploitation are reimbursed over a number of years;

(v) the IOC is remunerated for its services in cash in accordance with a formula; and

(vi) the IOC is authorized to buy and export a portion of the production at world price. However, in case of a national crisis this right may be curtailed.

Although the principal features of the Nigerian SCs are similar to those outlined above, it will be necessary to examine and assess some of their provisions. Before embarking on this exercise, let us briefly point out the differences between the production sharing and service contracts.

The PSC shares the usual features of duration, work obligations, etc., with the SC. The main differences between them lie in the mode for recovery of costs and the remuneration of the IOC. The distinctive feature of the SC is that the IOC is remunerated in cash and not in crude oil (although there may be provisions permitting the IOC to buy back the amount of crude oil at international prices from established production). Under the PSC, the IOC is remunerated by sharing with the HC in the quantity of crude oil produced. Thus, whereas the PSC involves an arrangement in which the IOC and the HC share in the oil produced in predetermined proportions, the SC involves the payment of a fee for services rendered.

3.2.d. The Nigerian Service Contracts (SCs)

The Nigerian SCs were entered into with a view to avoiding the less beneficial aspects of the PSC.[90] These include the high percentages of available crude oil set aside for "cost oil" and "tax oil", the windfall profits which may accrue to the IOC when there is an increase in the price of crude oil and the control of management and operational responsibilities by AON. Presently, there are eleven SCs in Nigeria between the NNPC and IOCs and each is for a duration of five years.[91] Their basic features include:

3.2.d.i. Rights and Obligations of the IOC (Contractor)

(a) The Provision of Funds

The IOC furnishes all the funds required for exploration and development and also the technical expertise needed for carrying out this obligation.[92] If there is no production (i.e. commercial discovery) during the contract term, the contract terminates and the IOC does not recover its costs.

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[90] Etikerentse, *supra*, note 19 at 47. Although the SC is the latest mode by which the IOCs can acquire oil rights in Nigeria, it still operates side by side with the *Petroleum Act* of 1969.

[91] Signed with Elf, Agip, Africa, and Nigus Petroleum Companies referred to in Omorogbe, *supra*, note 49 at 281.

(b) Reimbursement and Remuneration

The IOC is entitled to be reimbursed for exploration and development costs incurred if there is a commercial discovery within the contract area.[93] The IOC is also entitled to remuneration for services rendered.[94] Although the

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[92] Etikerentse, *supra*, note 19 at 47.

[93] Under the NNPC Proforma/Draft Service Contract of July 1979, reproduced in *Basic Oil Laws and Concession Contracts, South and Central Africa (Original Text), Supplement* Nos.56-60, (1979-1980), the method of reimbursement is as follows, *Article* 11.9:

$$Rq = \frac{EC + DC + Id}{4T}$$

Where Rq = Quarterly instalment.
EC = Total exploration costs.
Id = Total interest payable on development cost.
T = Repayment period in years.

Under *Article* 7.10, a commercial discovery is defined as: "The ratio of the present worth of the net earnings expressed in United States dollars to the projected quantity of petroleum won and save over the duration of the contract, expressed in cubic meters, yields a profit margin greater than 4.75."

[94] This is calculated in accordance with a formula. For example, under the NNPC Proforma/Draft Service Contract of July 1979, reproduced in *Basic Oil Laws and Concession Contracts, South and Central Africa (Original Text), Ibid.* remuneration is paid on the following basis:

$$Rqi = \frac{Dt \times Rm}{DT}$$

Where Rqi = Contractor's remuneration.
Dt = Contractor's total development costs expended on the commercial field to date.
DT = Contractor's total projected development costs to be expended on completion of the field development programme.

Rm = Quarterly remuneration due on completion of development programme.

IOC does not have title to the oil produced, it has the right to take its remuneration in kind and also the first option to buy back the crude oil produced from the contract area.[95] This option can be exercised even after the contract has expired, "thus guaranteeing the contractor a reliable source of crude oil supply in the event that a commercial discovery was made during the life of the contract."[96]

(c) Payment of Taxes

Tax is paid by the IOC, not under the provisions of the *Petroleum Profit Tax Act* 1959 *(as amended)*, but under the *Companies Income Tax Act* 1979. This is because under Section 2 of the *Petroleum Profit Tax Act* 1959 *(as amended)*, 28th Item, petroleum profit tax is payable by a company engaged in petroleum operation which is defined as: "The wining or obtaining....of petroleum in Nigeria....by a company on its own account...." Since under SCs the IOCs do not have title to the crude oil produced, they do not therefore, win or obtain petroleum on their own account.[97] On the other hand, petroleum profit tax is paid by the NNPC. There is a provision in the SCs for the NNPC to take over production activities after a period of three years from the date of commercial production.[98] This option has not yet been exercised by the

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[95] Etikerentse, *supra*, note 19 at 47. See also Omorogbe, *supra*, note 49 at 281.

[96] Etikerentse, *ibid*.

[97] *Ibid*.

[98] *Ibid*. at 48.

NNPC, although only Agip Energy has made a commercial discovery under a SC.[99]

(d) Training of Nigerians

Under SCs, the contractor is required to make use of Nigerian nationals to the maximum extent in all aspects of its operations.[100] Only in cases where specialised technical personnel are required and not available from among Nigerians, may the contractor with prior agreement of NNPC hire non-Nigerians, whose level of remuneration shall be approved by NNPC. However, the employment of non-Nigerians shall be subject to the condition that the

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[99] Omorogbe, *supra*, note 49 at 282.

[100] See *Articles* 4.1(g) and 14 of the NNPC proforma/Draft Service Contract, *supra*, note 93. In other service contracts in Nigeria, it is possible to find a schedule for training of local manpower to the following effect:

Skilled Category	By 3rd Year	By 5th Year	By 10th Year
Unskilled	100%	100%	100%
Skilled	50%	75%	100%
Clerical & Supervisory	50%	75%	90%
Technical	50%	75%	85%
Management	50%	75%	85%

Source: K. Khan, *supra*, note 47 at 18.

The main objective of these provisions concerning manpower training, is to enable Nigerians to control and operate all phases of the oil industry. Despite these requirements, Nigerians have not succeeded in exercising *de facto* control over the oil industry. The training and employment of Nigerian personnel in petroleum technology would result in the acquisition of petroleum technology from the IOCs. If the objective of the government is to be achieved, the government must also be directly involved in the training of Nigerian personnel.

contractor undertakes to train Nigerians in corresponding specialisation to replace such non-Nigerians in the shortest possible time. The contractor shall within six months after the effective date and after consultation with NNPC submit for NNPC's approval a detailed recruitment programme, and within twelve months, submit for NNPC's approval, a training programme for all Nigerians employed by the contractor in the conduct of all petroleum operations, in accordance with the *Petroleum Act* 1969.

(e) Exploration Programme and Budget

Under SCs, the contractor shall prepare with respect to each financial year, and submit to NNPC for its approval programmes and budgets for exploration in the contract area.[101] Such programmes and budgets shall be such as to ensure the complete fulfilment of the minimum exploration obligations assumed by the contractor under the provisions of the contract.

The programme and budget for exploration for the period between the effective date and the end of the financial year in which the effective date falls shall be submitted not later than three months from the effective date. The NNPC and the contractor shall meet within thirty days after the submission of each exploration programme and budget proposal to approve or revise the same. In the event that the parties fail to approve such programme and budget at such meeting, the parties shall meet not later than fifteen days from the date of that programme and budget to reconsider the programme and budget, with amendments thereto. If the parties still do not mutually approve such programme and budget proposal, then the contractor's proposal, with mutually agreed amendments if any, shall be deemed to be the approved programme and budget for the contract area.

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[101] See *Article* 6 of the NNPC proforma/Draft Service Contract, *ibid*.

3.2.d.ii. An Assessment

The SC represents the effort by HCs to enlist the intervention of risk-taking IOCs while, at the same time, theoretically affirming the principle of permanent sovereignty over their natural resources.[102] In terms of achieving the objective of *de facto* control of their oil industry, SCs are more advantageous to HCs when compared with the PSCs. This is clearly brought out by the provision contained in SCs for the HC's national oil company to take over the production activities in the event of commercial production after a specified period.

In addition, in SCs, the cost recovery and remuneration terms for the IOCs are more favourable to the HC than those of the PSC and the SCs are of much shorter duration.[103] Despite these advantages, it has been argued that the SCs have not fully succeeded in shifting *de facto* control from the IOCs to the HCs and that in this respect, they are not very different from the other forms of contractual arrangements.[104] According to Asante:[105]

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[102] Blinn, *supra*, note 1 at 97. See chapter 4 for further discussion of the principle of permanent sovereignty over natural resources.

[103] Omorogbe, *supra*, note 49 at 282.

[104] Asante, *supra*, note 21 at 369.

> If the service contract continues to vest exclusive management and control in the transnational corporation, an essential ingredient of the traditional concession regime will persist, notwithstanding the fact that under the contract the state is deemed to be owner of the natural resource at the point of extraction.

This statement is correct, though, as opposed to a concession, the NNPC can insist on its rights at anytime. It is further argued that the adoption of new and sophisticated legal arrangements must in addition, be backed up by political and economic measures.[106] The primary objective of HCs should be the acquisition of basic technological and managerial skills. The training and employment of skilled Nigerian personnel into top management positions in the IOCs are two first steps which have been recommended.[107] Both policies, over time, would generate a pool of Nigerians capable of exercising *de facto* control of the oil industry.

It must be stressed that the above assessment of the production sharing and service contracts is not to make a case against such arrangements. Apart from the possible financial benefits, the production sharing and service contracts, when properly monitored, could serve as useful mechanisms for management and technical training.[108] They could also provide access to the

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[105] *Ibid*. at 362.

[106] *Ibid*.

[107] S.K.B. Asante & A. Stockmayer, "Evolution of Development Contracts: The Issue of Effective Control" in *Legal and Institutional Arrangement in Mineral Development* (London: Mining Journal Books, 1982), 53 at 61.

[108] Asante, *supra*, note 21 at 357.

operational strategies, policies, and technical skills of the IOCs.[109] This assessment is only meant to point out some of the dangers inherent in the assumption that a change in the nomenclature relating to oil agreements has meant that the government's objectives have been achieved. The production sharing and service contracts must now be viewed as economic development agreements rather than as mere contracts.[110] It is only then that the development issues of training and employment of skilled Nigerian personnel can be addressed.

In addition, these contractual arrangements should be revised continuously until an arrangement is achieved which is capable of securing the HCs objectives.[111] According to Hossain:[112]

> The task of establishing a good legal framework involves not the mechanical imitation of standard precedents, but the imaginative and resourceful putting together in a package of mechanisms which have proved to be the most effective to secure certain general objectives....

Although the SC has secured increased financial returns and a greater degree of control of its oil industry for the HC than the traditional concession, it still involves the sale of the transnational corporation's risk capital and technical, managerial, and marketing expertise.[113] The introduction of contractual joint ventures for predominantly political reasons, without adequate consideration of how to acquire the necessary technology for the oil industry, and thus, *de facto* control, affected subsequent economic development in several HCs, including Nigeria during the 1970s.[114]

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[109] *Ibid.*

[110] D.N. Smith, *New Eyes for Old: The future, Present and Past in the Evolution of Mineral Agreements* (Lagos: Nigerian Institute of Advanced Legal Studies, 1981) at 8.

[111] Hossain, *supra*, note 2 at 175.

[112] *Ibid.* at 176. See also C.R. Blitzer, P.E. Cavoulascos & J.L. Paddock, "Risk Bearing and Contract Design: Are Stable Contracts Feasible" in K. Khan ed., *Petroleum Resources and Development-Economic, Legal and Policy Issues for Developing Countries*, *supra*, note 11 at 173, where it is argued that both countries and companies have been too conservative in their approach to contract design. Conservative means that they have been reluctant to move outside the conventional framework, to create the contract form most suitable to a particular situation, rather than using a structure which has been used perhaps successfully, by another country.

3.2.e. Conclusion

No doubt, the decade of the 1970s witnessed a number of significant advances in government participation in the oil industry. Yet, this apparent evolution of oil contracts into the new forms of contractual joint ventures has not secured for the government the technological capabilities which would enable it to achieve its main objective of control over the oil industry. The absence of *de facto* control by Nigeria over the oil industry calls into question the compatibility of the modes of acquisition of oil rights with the principle of permanent sovereignty over natural resources. *De facto* control of the oil industry can be achieved by the training and employment of Nigerian personnel into top management positions in the IOCs.[115] This, together with the formulation of a clear oil policy to guide management would go a long way towards the realization of the government's objectives.

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[113] Asante, *supra*, note 21 at 363. See however, T. Walde, "Third World Mineral Development in Crisis - The Impact of the World Recession on Legal Instruments Governing Third World Mineral Development" (1985) 19 J.W.T.L. 3 at 11, where the writer points out that: "A comparative analysis of the various types of agreement has found that, from a financial view point, the form of the agreement is of little importance and that states often may have even lost revenues through the "innovative arrangements" advocated in the 1970s" and also Omorogbe, *supra*, note 49 at 283 that "the service contract has made little difference to the Nigerian legal framework...."

[114] R. Kemper, " The Concept of Permanent Sovereignty and its impact on Mineral Contracts" in *Legal and Institutional Arrangements in Mineral Development, supra*, note 107, 29 at 33. It has been argued, that state participation in the oil industry has not resulted in any radical changes in the pattern of behaviour of the 1OC. See E.J. Usoro, "Foreign Oil Companies and Recent Nigerian Petroleum Oil Policies" (1972) 14 Nigerian J.E.S.S. 301 at 304. All modern oil contracts illustrate that ownership does not automatically imply effective control and that the function of management can be separated from ownership. On this point see Walde, *ibid.* at 13.

It appears that the problem is not restricted to the absence of well defined governmental objectives, but where such objectives exist, there is the associated problem of implementation.[116] A well "structured joint-venture"[117] is, however, capable of providing a balance of "mutual equivalence of contractual advantages" between the HCs and IOCs.[118] This approach to oil development contracts will enable the HC to derive greater benefits by controlling its oil industry and, thus, to serve its economic development purposes.[119] The IOC, on the other hand, is allowed a reasonable return on its investment under conditions of economic and legal security.[120]

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[115] This has been discussed extensively in section 2.3.e. of chapter 2.

[116] H.G. Broadman & E.J. Wilson 111, "Trials and Tribulations of Third World Petroleum Development: Lessons and Advice for Prospective Producers in K. Khan ed., *Petroleum Resources and Development*, *supra*, note 11, 262 at 262-263.

[117] It has been argued that a joint-venture must take into account which of the parties has a comparative advantage in bearing the risk associated with oil exploration and exploitation. This comparative advantage will depend on which party has the ability to diversify the risk and that this approach would lead to a more efficient allocation of investment and ensure contractual stability. See Blitzer, Cavoulacos & Paddock, *supra*, note 112 at 174. In most cases the IOCs have the money and technical skills which are required and are sufficiently diversified, so that they can afford risks. However, the government of HCs have neither large amount of capital or trained manpower and hence cannot afford the risk of oil exploration capital. It is, therefore, argued that the government of the HC should not embark on an oil exploration programme, but rather should leave it to the IOCs. For a contrary view see M. Tanzer, *The Political Economy of International Oil and the Underdeveloped Countries* (Boston: Beacon Press, 1969) at 133-135.

[118] M. Mughraby, *Permanent Sovereignty Over Oil Resources* (Beirut: Middle East Research and Publishing Centre, 1966) at 190.

In the next section, we shall examine the problem of contractual stability and how the rights acquired by the IOCs under production sharing and service contracts can be adjusted when changes occur in the oil industry. It would be argued that renegotiation clauses may assist HCs in achieving their objectives.

3.3. Contractual Stability

The issue of contractual stability represents a major source of conflict between IOCs and HCs. On the one hand, the IOCs are more concerned with stability and predictability in their contractual relations with the HCs, while the HCs favour a more flexible contractual regime on the other.[121] The IOCs, therefore, invoke the principle of sanctity of contract (*pacta sunt servanda*). The legal consequence of this reasoning is that the HC is not entitled unilaterally to modify or terminate the contract with the IOC.[122] The practical effect is that the contract cannot be renegotiated or reviewed. The HCs counter this argument by relying on the principle of permanent sovereignty over natural resources [123] and the charter of economic rights and duties of states under which they claim that these contracts are governed by their municipal laws and, therefore, subject to unilateral change. It is submitted that excesses of formalism have failed to properly address some crucial issues, such as how changes in circumstances should be dealt with in contracts between IOCs and HCs.[124] It will be contended that a properly drafted renegotiation clause can effectively protect the interests of both the IOCs and the HCs and, thus, prevent any potential conflict.[125] These clauses are preferable to stabilization clauses because their flexibility may enable HCs to achieve their objectives. Let us briefly examine these two clauses.

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[119] *Ibid.*

[120] *Ibid.*

[121] See S.K.B. Asante, "Stability of Contractual Relations in the Transnational Investment Process" (1979) 28 I.C.L.Q. 401 at 404. The author's views are also expressed in "The Concept of Stability of Contractual Relations in the Transnational investment Process" in K. Hossain ed., *Legal Aspects of the New International Economic Order* (New York: Frances Pinter (Publishers) Ltd., 1980), 234.

[122] Asante, *ibid.* at 405.

3.3.a. Stabilization Clauses

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[123] There is disagreement as to whether oil investment contracts are governed by international law or the municipal law of the host state. That the law applicable to oil investment contracts is the municipal law of the host state, is widely supported by the developing countries.It is argued that a contract which is not a contract between states in their capacities as subjects of international law, is based on the municipal of some country. See the *Serbian and Brazilian Loans Cases*, P.C.I.J. Series A. No. 20/21 (1929) at 41, Lord McNair, "General Principles of Law Recognized by Civilized Nations" (1957) 33 B.Y.I.L. 1 at 10 and Sornarajah, *infra*, note 130 at 195. The principle of internationalization of oil investment contracts is supported by most writers from the developed countries. It is argued by these writers, that the conclusion of an oil investment contract by a state with a foreign private investor, does not essentially differ from the conclusion of a *treaty* as an act creating legal obligation. See F.A. Mann, "The Proper Law of Contract Concluded by International Persons" (1959) 35 B.Y.I.L. 34 and W. Friedmann, "The Relevance of International Law to the Processes of Economic and Social Development" in R.A. Falk & C.E. Black eds., *The Future of International Legal Order: Wealth and Resources* Vol. 2 (Princeton, New Jersey: Princeton University Press, 1970) 3 at 21-27.

[124] Asante, *supra*, note 121 at 407-408.

[125] W. Peter, *Arbitration and Renegotiation of International Investment Agreements* (Dordrecht, Netherlands: Martinus Nijhoff Publishers, 1986) at 146.

The purpose of stabilization clauses is essentially to protect the investment and interest of IOCs from the spectre of unilateral change of the law of the HC and, thus, to ensure that the contract would not be altered, but remain stabilized. The use of stabilization clauses is, therefore, an affirmation of the principle of *pacta sunt servanda.* [126] Stabilization clauses take several forms, which may include one or more of the following:[127]

> (a) It may simply provide that the IOC's rights will remain unaffected by subsequent legislation;
>
> (b) it may provide that the agreement will prevail over future legislation or regulation if there is any inconsistency between the two (the "anti-inconsistency rule"); [128] and
>
> (c) the municipal law of the HC may be incorporated into the contract and "frozen" at that specific date. This is the most far-reaching form a stabilization clause may take.[129]

Sornarajah has suggested that stabilization clauses are invalid in the light of the principle of permanent sovereignty over natural resources. He said:[130]

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[126] *Ibid.* at 136.

[127] *Ibid.* at 136-137. See also Blinn, *supra*, note 1 at 302-306 and G.R. Delaume, *Law and Practice of Transnational Contracts* (New York: Oceana Publications Inc., 1988) at 45-46.

[128] Peter, *ibid.* at 137.

[129] *Ibid.* at 140.

[130] M. Sornarajah, "The Myth of International Contract Law" (1982) 16 J.W.T.L. 187 at 210. See also E.J. Arechaga, "Application of the Rules of State Responsibility to the Nationalization of Foreign-Owned Property" in K. Hossain ed., *Legal Aspects of the New International Economic Order*, *supra*, note 121, 220 at 229-230. He said regarding stabilization

> In the theory underlying the principle, sovereignty over natural resources resides in the people....Thus, the acceptance of the principle creates a constitutional limitation on the state in international law to deal with its natural resources, except in accordance with the interests of its people. *This would mean that a state cannot validly agree not to change the terms of the agreement on the exploration of natural resources....* (Emphasis is mine)

However, continuous state practice, as well as recent arbitral decisions, have continued to confirm the validity of stabilization clauses.[131] A contrary view often expressed is that when a state makes commitments in a stabilization clause, it "does so, not in derogation of, but in the exercise of the same sovereignty which inheres in it."[132] It was thus, held in *Government of Saudi Arabia* v. *Arabian American Oil Company* [133] that "nothing can prevent a state from binding itself irrevocably....and from granting to the concessionaire irretractable rights."[134] In the Libyan nationalization cases,[135] the

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clauses:"This runs counter to the fundamental concept and purpose of the permanent sovereignty of a state over its natural resources and wealth proclaimed in the Charter and in other General Assembly resolutions." The same view is expressed by the author in (1978) 1 *Recueil des Cours* 297 at 297. For a contrary view see Professor Weil referred to by Arechaga at 229-230. Note however, that Professor Weil's conclusion is based on his view that oil contracts containing stabilization clauses are govern by international law and not the law of the HC.

[131] Peter, *supra*, note 125 at 141.

[132] S.R. Chowdhury, "Permanent Sovereignty and its Impact on Stabilization Clauses, Standards of Compensation and Patterns of Development Co-operation" in K. Hossain and S.R. Chowdhury eds., *Permanent Sovereignty over Natural Resources in International Law* (New York: St. Martins Press, 1984), 42 at 47.

[133] (1963) 27 I.L.R. 117. [Hereinafter *Aramco*].

[134] *Ibid.* at 168.

[135] *Texaco Petroleum Company Ltd. and California Asiatic Oil Company* v. *The Government of Libya* (1979) 53 I.L.R. 398, [hereinafter *Topco*], *British Petroleum Company* v. *The Government of Libya* (1979) 53 I.L.R. 297, [hereinafter *BP* v. *Libya*] and *Libyan American Oil*

stabilization clause provided that:[136]

> (i) The Government of Libya, the commission and the appropriate authorities will take all steps necessary to ensure that the company enjoys all the rights conferred by this concession. *The contractual rights expressly created shall not be altered except by mutual consent of the parties. (ii) This concession shall throughout the period of its validity be construed in accordance with the petroleum law and the regulations in force on the date of the execution of the agreement by which this paragraph (2) was incorporated into this Agreement. Any amendment to or repeal of such Regulations shall not affect the contractual rights of the company without its consent.* (Emphasis is mine).

The decisions of the arbitrators [137] in the Libyan cases reflect their different views as to the legal effect of stabilization clauses on the principle of permanent sovereignty over natural resources. In *BP* v. *Libya* the arbitrator held that despite the stabilization clause, the nationalization was effective.[138] In the *Liamco* case, the arbitrator went further and concluded that the United Nations resolution on permanent sovereignty over natural resources, if not a source of law, is evidence of the recent dominant trend of international opinion concerning sovereign right of states over natural resources.[139] However, in

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Company v. *The Government of Libya* (1981) 20 I.L.M. 1, [hereinafter *Liamco*].

[136] *Clause* 16.

[137] In the *Topco* case, the arbitrator Professor Dupuy held that: "The result is that a state cannot invoke its sovereignty to disregard commitments freely undertaken through the exercise of the same sovereignty and cannot, through measures belonging to its internal order, make null and void the rights of the contracting party which has performed its various obligations under the contract". However, in *BP* v. *Libya* and *Liamco*, the arbitrators held the stabilization clauses to be legally ineffective to nullify the nationalization measures.

[138] *Supra*, note 135 at 353.

[139] *Supra*, note 135 at 103.

the *Topco* case, the arbitrator dismissed this resolution as having no binding effect in international law.[140] In the recent award in *Government of Kuwait* v. *American Independent Oil Company* [141] a different conclusion was arrived at. The stabilization clause provided that:[142]

> The Shaik shall not by general or special legislation or by administrative measures or by any other act whatever annul this Agreement....No alteration shall be made in the terms of this Agreement by either the Shaik or the company except in the event of the Shaik and the company jointly agreeing that it is desirable in the interest of both parties to make certain alterations, deletions or additions to this Agreement.

The majority decision of the tribunal has been summarized as follows:[143]

> (i) A stabilization clause has to be interpreted restrictively, and should be construed to provide protection only against a measure having a confiscatory character;
>
> (ii) an act of nationalization is not a confiscatory action, as long as compensation is paid, and hence does not fall within the scope of the stabilization clause; and
>
> (iii) a stabilization clause is normally conceived as a temporary limitation providing a protection which could be justified if limited to a relatively short period, but if imposed for a long period such

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[140] *Supra*, note 135 at 483-495.

[141] (1982) 21 I.L.M. 976. [Hereinafter *Aminoil*].

[142] *Article* 17.

[143] A.S. El-Kosheri & T.F. Riad, " The Law Governing a New Generation of Petroleum Agreements: Changes in the Arbitration Process" (1986) 1 ICSID Rev. 257 at 283.

as sixty years, becomes a generalized restriction hardly compatible with the inherent powers of the state.

In a minority opinion, Sir G. Fitzmaurice stated that, although the nationalization measure undertaken by the government of Kuwait was perfectly lawful as an act of state, it was nevertheless irreconcilable with the stabilization clause.[144] This minority opinion is correct. The legal power of a state to change the destination or the method of exploitation of its natural resources, whatever arrangements may have been made for their exploitation by a previous government either by treaty or contract, is now well recognized.[145] However, in the exercise of this legal power, a state may be found liable for a breach of contract for which damages may be awarded.[146]

Although stabilization clauses represent a "valuable bargaining chip" to the IOCs, they cannot cure the inherent instability of these oil contracts, and may, in certain instances, lead to conflict between HCs and the IOCs.[147] Despite their rigidity, stabilization clauses can still be found in international oil contracts between HCs and IOCs. It is submitted that since *de facto* control of the oil industry in several HCs is still in the hands of the IOCs, the continued use of stabilization clauses may prevent HCs from securing *de facto* control of their oil industries during the period the contract is stabilized. A HC that disregards a stabilization clause in its contract with an IOC in its quest for control of its oil industry, may be found liable for breach of contract and be ordered to pay damages to the IOC. It is, therefore, not surprising that HCs prefer a more flexible mechanism which enables them to adjust their contract with the IOCs in their quest for increased control of their oil industry.

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[144] Peter, *supra*, note 125 at 143-144.

[145] See Sornarajah, *supra*, note 130, Arechaga, *supra*, note 130 and G. Elian, *The Principle of Sovereignty Over Natural Resources* (Netherlands: Sijthoff & Noordhoff, 1979) at 10-11.

[146] See the Libyan cases, *supra*, note 135. In *Liamco* and *BP* v. *Libya*, the arbitrators held that nationalization was arbitrary and awarded damages. However, in *Topco*, the arbitrator ordered *restitution in integrum*.

[147] Peter, *supra*, note 125 at 146. See also R. Brown, "The Relationship between the State and the Multinational Corporation in the Exploitation of Resources" (1984) 33 I.C.L.Q. 218 at 223, where the writer submits that stabilization clauses are "a fruitful source of provocation and misunderstanding."

In Nigeria, modern contractual agreements in the oil industry do not utilize stabilization clauses. On the contrary, it is specifically provided in the PSC and SCs that no term or provision of these contracts, including the agreement of the parties to submit to arbitration, shall prevent or limit the Government of Nigeria from exercising its inalienable rights. It follows, therefore, that the Nigerian government can unilaterally alter or abrogate its contract with the IOCs, but liability for breach of contract would arise, for which damages may be awarded.

3.3.b. Renegotiation Clauses

Renegotiation clauses are an expression of contractual stability and provide an effective alternative to outright nationalization.[148] The renegotiation of international agreements is possible in international law under the principle of *clausula rebus sic stantibus*, which states that a fundamental change in basic circumstances of a contract justifies a revision.[149]

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[148] Peter, *ibid*. See also Chowdhury, *supra*, note 132 at 55.

Although the HC is more likely to invoke the renegotiation clause first, it is also available to IOCs seeking to change the agreement in times of recession and depressed prices and it can, thus, be an effective means of stabilizing the contract.[150] It is also possible for HCs and the IOCs to restrict renegotiation clauses to a particular subject matter, such as taxes or royalties, by providing for renegotiation, for example, after five years from the date of the conclusion of the agreement. If properly restricted, renegotiation clauses are "stabilization clauses that differ from real stabilization clauses by their limited effect of stabilization in time or with regard to substantive matters."[151] The "triggering events" for renegotiation may also be chosen by parties as indicative of the possibility of renegotiation, as in the following example:[152]

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[149] On this point, see H.S. Zakariya, "Changed Circumstances and the Continued Validity of Mineral Development Contracts" in K. Hossain ed., *Legal Aspects of the New International Economic Order, supra*, note 121, 263 at 274. The author argues that: "*Pacta sunt servanda* should of course continue to enjoy the respect and adherence due to it as an essential vehicle of stability and security without which no legal order can properly be maintained. But legal order should equally ensure equity and justice. This can only be achieved through the rational application of such principles as *rebus sic stantibus*". See also R. Geiger, "The Unilateral Change of Economic Development Agreement" (1974) 23 I.C.L.Q. 73 at 86, where the author said: "Even in the field of treaty relations the principle of sanctity of contract is not absolute. Long term economic co-operation between equal partners....require a higher degree of flexibility. To say that such contracts are in all but extreme circumstances binding makes the breach more likely....(he continued at 104) "Economic development agreements cannot be understood as a rigid scheme of rights and duties, but rather as a frame of reference for future relations. They are of prospective character and therefore must provide a certain degree of flexibility. Their success essentially depends on mutual confidence and co-operation between the parties." For further readings see M. Sornarajah, "The Climate of International Arbitration" (1991) 8 No.2 J.Int'l. Arb. 47 at 65-66 and OPEC Declaratory Statement of Policy of 1968 (Resolution XVI.90). One of its ten principles reads as follows:"....Government may acquire a reasonable participation, on the ground of the principles of changing circumstances...." See *OPEC Official Resolutions and Press Releases* (1960-1990) at 62.

[150] Peter, *supra*, note 125 at 154.

[151] *Ibid.* at 147.

> In case of *profound change in the circumstances* existing at the effective date of this contract, the parties, at the request of any one of them, will consult together for the purpose of reconsidering such changes in or clarifications of this Mineral Concession Agreement as the parties deem to be appropriate.

The effectiveness of renegotiation clauses in meeting changing circumstances in the world oil market cannot be overemphasised. Reduction in oil prices due to oversupply in the market as well as the unexpected price rise may call for renegotiations. Renegotiation of existing oil agreements constitutes a more subtle and flexible way to adapt a relationship to change.[153] Recent practice demonstrates that renegotiation is a natural accommodation of partners in long-term business relations.[154] According to Walde:[155]

> The crucial issue of negotiation of long-term agreements is to strike the balance between the predictability of contractual commitments necessary to find long-term financing for large scale mineral projects and the interest of partners not to assume long-term, fixed-price and fixed-quantity obligations that might prove excessively onerous or excessively profitable to one party in the

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[152] *Ibid.* at 155. The most important category of renegotiation triggers is the host country adoption of policies to promote economic or political goals. Examples would include measures to advance socialism or state ownership. See W.A. Stoever, *Renegotiations in International Business Transactions: The Process of Dispute - Resolution between Multinational Investors and Host Societies* (Lexington, Massachusetts: D.C. Heath & Co., 1981) at 309.

[153] Walde, *supra*, note 113 at 25 and Chowdhury, *supra*, note 132 at 56. Renegotiation of contractual arrangements is sanctioned by OPEC. See OPEC Declaratory Statement of Policy of 1968 in *OPEC Official Resolutions and Press Releases*, *supra*, note 149 at 62, where it is provided that: "Notwithstanding any guarantee of fiscal stability that may have been granted to the operator, the operator shall not have the right to obtain excessively high net earnings after taxes. The financial provisions of contracts which actually result in such excessive high net earnings shall be open to renegotiation."

[154] Walde, *ibid.* at 25-26.

[155] *Ibid.* at 26.

> case of a fundamental change of economic conditions. It is clear that the notion of "sanctity of contract", born in the liberal economy of the last century....is giving way to a more fluid, less predictable....notion of the agreement as an institutional and procedural framework of long-term co-operation.

It is also possible for HCs and the IOCs to maintain a flexible pricing arrangement, while at the same time maintaining a stable contractual arrangement. It must however, be pointed out that there are inherent dangers in excessive flexibility, particularly in respect of pricing arrangements. Excessive flexibility in pricing arrangements may lead to constant changes to the price of crude oil and may affect the pace of exploration and production of oil and, therefore, its demand and supply.

Presently, there are no renegotiation clauses in the contractual arrangements currently in use in Nigeria's oil industry. However, it has been possible for the government and the IOCs to renegotiate certain aspects of their agreements. For example, following the unprecedented oil glut and low prices in 1986, and the consequential drop in exploration activities, it became necessary for the Nigerian government to sign a memorandum of understanding (MOU) with the IOCs.[156] The MOU between the Nigerian government and the IOCs contains all the advantages of renegotiation clauses, as it makes it possible for the parties to renegotiate the terms of their agreement when circumstances change. Although the MOU between the government and the IOCs has worked well, renegotiation clauses may sometimes fail to achieve their purpose and, thus, result in acrimony between HCs and IOCs.[157]

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[156] The MOU was amended in 1991. See Press Statement by the Minister for Petroleum Resources, *supra*, note 51. Renegotiation Agreements between the Nigerian government and IOCs is not a new phenomenon. See Text of Revenue Renegotiation Agreement between the Nigerian government and the IOCs, signed in May 1971 in *Basic Oil Laws and Concession Contracts, South and Central Africa (Original Text), Supplement* Nos.31-35.

Recent trends in the natural resources industry reveal the increasing use of renegotiation clauses because they are mutually beneficial to the interests of HCs and the IOCs.[158] Although it is difficult to recommend a particular renegotiation clause, a properly drafted clause that utilizes the "triggering event" provision, is capable of reconciling the conflicting principles of *pacta sunt servanda* and *clausula rebus sic stantibus.* The importance of negotiations in achieving the government's objective of increased revenue from the oil industry cannot be overemphasised. For example, equity participation in Nigeria's oil industry which resulted in increased revenue for the government was achieved mainly through negotiations with the IOCs.[159] It is further submitted that renegotiation clauses in oil contracts can, similarly, assist the government in securing its other objectives; which include, control over operations, and the development of national capabilities in the field of petroleum operations. As an American expert put it, a modern investment contract is only

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[157] See the renegotiations between the government of Kuwait and American Independent Oil Company. Renegotiation was provided for under *Article* 9 of the 1948 agreement between the parties. After the renegotiations ultimately failed in September 1977, the property of American oil company was nationalized. It seems however, that the renegotiations failed because the government of Kuwait had made up its mind to take over full ownership of its oil resources. See Peter, *supra*, note 125 at 70-71.

[158] Chowdhury, *supra*, note 132 at 56. In Canada, the *change of law clause* referred to in section 3.1.a. above, serves the purposes of a renegotiation clause.

[159] See section 2.3. of chapter 2.

"an invitation to a ball."[160] If there is no flexibility in the contract, acrimonious relationships could develop between the parties. The existence of renegotiation clauses make harmonious relations between the parties possible and would enable the IOCs to keep the objectives of the HC in mind in pursuing their profit objectives.[161]

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[160] D.N. Smith & L.T. Wells, "Conflict Avoidance in Concession Agreements" (1976) 17 Harv. J.I.L. 51.

[161] Sornarajah, *supra*, note 130 at 214-215.

Chapter 4

THE PRINCIPLE OF PERMANENT SOVEREIGNTY OVER NATURAL RESOURCES AND ITS CONTRIBUTION TO THE MODES OF ACQUISITION OF OIL RIGHTS

4.0. Introduction

In chapter 1, a brief mention was made of the influence of the United Nations resolution on permanent sovereignty over natural resources and how this resolution helped to shift the balance of power from the international oil companies (IOCs) to the developing countries. It was also asserted in chapter 1 that this resolution rejected the idea of investor ownership and control of a state's natural resources and was one of the factors leading to the abandonment of the traditional concession.

In section one of this chapter, an examination will be undertaken of the origin and development of the principle of permanent sovereignty over natural resources. Section two examines the legal status of the resolutions on permanent sovereignty over natural resources, while in section three the contribution of the principle and its compatibility with the modes of acquisition of oil rights is examined.

In addition, this chapter elucidates the meaning of the principle as formulated by the United Nations General Assembly resolutions. It will be argued that the principle gave a strong impetus to the developing countries and provided a basis on which they could claim to alter inequitable legal arrangements under which foreign investors enjoyed rights to exploit natural resources found within their territories. It is however, doubtful whether the present modes of acquisition of oil rights in Nigeria are compatible with the principle. The justifications for selecting the principle for judging the merit of the modes of acquisition of oil rights in Nigeria are as follows:

(i) The principle of permanent sovereignty over natural resources is theoretically affirmed in section 1(1) of the *Petroleum Act* of 1969 and also in section 40(3) of the *Federal Constitution of Nigeria* 1979;[1] and

(ii) it was the principle that inspired the present modes of acquisition of oil rights in Nigeria.

4.1. The Origin and Development

The principle of permanent sovereignty over natural resources was first raised by the Chilean delegation at the Eighth Session of the Human Rights Commission, when it was working on the preparation of the Draft International Covenants on Human Rights in pursuance of General Assembly Resolution No. 545 (VI) of February 5, 1952.[2] In this Resolution, the General Assembly decided to include the right of all peoples and nations to self-determination as part of the Human Rights Covenants and requested the Commission to prepare a draft on the subject.[3] After a long discussion, the Commission's working party agreed to include in the draft covenants the following paragraph:[4]

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[1] This has been discussed in section 2.1. of chapter 2.

[2] S.K. Banerjee, "The Concept of Permanent Sovereignty Over Natural Resources" (1968) 8 Indian J. Int'l Law 515 at 517.

[3] *Ibid.*

> The right of the people to self-determination shall also include permanent sovereignty over their natural wealth and resources. In no case may a people be deprived of its own subsistence on the ground of any rights that may be claimed by other states.

Once the principle was linked with self-determination, it became directly involved with the colonial issue, and the debate in the United Nations became polarised between the developed, capital-exporting countries and the developing, capital-importing countries.[5] Historically, therefore, the principle of permanent sovereignty over natural resources is a logical outcome of the principle of self-determination which brought about the dissolution of the colonial empires after the second world war.[6] After attaining political independence, most developing countries soon realised that political independence was meaningless if foreign control endured in the economic sector, all the more so since for most developing countries their natural resources generally represented their only economic assets.[7]

It was, therefore, not surprising that the objectives which the developing countries established for their natural resources conflicted with the interests of foreign based companies in protecting their usually advantageous investment conditions.[8] The history of the principle of permanent sovereignty over natural resources can, therefore:[9]

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[4] J. Baloro, "Some International Legal Problems Arising From the Definition and Application of the Concept of Permanent Sovereignty Over Wealth and Natural Resources of States" (1987) 20 CILSA 335 at 335.

[5] Banerjee, *supra*, note 2 at 515.

[6] M. Sornarajah, *The Pursuit of Nationalized Property* (Dordrecht, Netherlands: Martinus Nijhoff Publishers, 1986) at 120.

[7] R. Kemper, "The Concept of Permanent Sovereignty and its Impact on Mineral Contracts" in *Legal and Institutional Arrangements in Mineral Development* (London: Mining Journal Books, 1982), 29 at 30.

> Be seen as the history of the struggle between private foreign investment and the interests of the capital-exporting countries on the one side and the interests of the capital-importing countries and their economic and development goals on the other side.

The main controversy over the principle of permanent sovereignty over natural resources was whether, in the exercise of that right, states were also obliged to act in accordance with the governing principles of international law.[10] Most developing countries asserted that sovereignty meant, *inter alia*, the freedom of the state to exploit and dispose of its natural resources, unrestrained by any political, economic or legal limitations imposed or maintained by an external authority.[11] According to these developing countries, a state cannot attain economic independence until it is able to control its natural wealth and resources.[12] This economic aspect of sovereignty is important because it enables the developing countries to carry out their development plans and raise their standard of living. Emancipation from economic colonialism was still required for many developing states.[13] The right of a state to dispose of its natural resources was a natural right, an inalienable right, an absolute right, a permanent right, according to spokesmen of developing countries.[14] Thus, the concept of sovereignty over natural resources, as conceived of by the capital-importing countries, was "in the nature of Austin's sovereign, absolute and unqualified by any limitations of international responsibility."[15]

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[8] *Ibid.*

[9] *Ibid.*

[10] Banerjee, *supra*, note 2 at 542.

[11] M.S. Rajan, *Sovereignty over Natural Resources* (New Jersy: Humanities Press, 1977) at 136.

[12] *Ibid.*

While some developing countries spoke of sovereignty in absolute terms, many of them expressly and repeatedly affirmed their respect for all contracts with foreign firms or governments freely entered into.[16] These countries were not oblivious to the need for foreign investment, if it were available on mutually agreeable terms.[17] They were also perfectly conscious of the compelling needs of inter-dependence of nations and had no desire to encourage economic isolation which might be counter- productive to their national interests.[18] A claim of unlimited sovereignty by some developing countries bears a severe economic risk, irrespective of the understandable political reasons for these demands.[19] There was the danger that the developing country, flushed with its new power, might have forced its leverage to a point where it would inevitably come to suffer in the long run.[20] For example, the claim for unlimited sovereignty might severely affect the flow of foreign investment to a developing country.

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[13] *Ibid.*

[14] *Ibid.* See also G. Elian, *The Principle of Sovereignty Over Natural Resources* (Netherlands: Sijthoff & Noordhoff, 1979) at 12, where the author said: "The universal constant for all states - the relation almost universally - acknowledged as a general truth - is that of sovereignty over their resources. The state's definitive, indisputable and uncontested supremacy over its territory involves a reality which is beyond discussion: Permanent sovereignty over the resources of that territory."

[15] Banerjee, *supra*, note 2 at 516.

[16] Rajan, *supra*, note 11 at 138.

[17] *Ibid.*

[18] *Ibid.* at 139.

The developed countries, on their part, argued that while territorial sovereignty was a legal attribute of every state, it was limited by the duties and obligations imposed on states by international law and by the economic and political necessities imposed by the growing inter-dependence of states.[21] They therefore, did not think it worthwhile to spend much time on proclaiming it, affirming it and elaborating it - like the spokesmen of the developing countries.[22] The attitudes of the developing and developed countries did not appear to be irreconcilable - apart from the fact that some developing and developed countries expressed views which cut across the general, dominant attitude of the groups to which they belonged.[23] According to Rajan:[24]

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[19] Kemper, *supra*, note 7 at 34.

[20] *Ibid*.

[21] Banerjee, *supra*, note 2 at 516.

[22] Rajan, *supra*, note 11 at 142. See also Baloro, *supra*, note 4 at 352, where the writer asserts that: "From the point of view of public international law, the concept of permanent sovereignty over wealth and natural resources of states refers to the already existing rights of states to expropriate or nationalize foreign property within their territorial jurisdiction."

[23] Rajan, *ibid*. at 144.

> They are speaking about the same concept, but only from two different ends of the same spectrum of interdependence which connects them together, and on the same common basis of membership of the United Nations, namely 'sovereign equality'....The only difference - largely and only apparently - seems to be that the developing states emphasize - not exclusively however - their rights, while the developed states emphasize - again, not exclusively - the obligations of sovereignty incumbent on both groups of states. Both of them equally recognize the compulsions of interdependence and international co-operation in mutual interest.

The reasons for this difference of opinion are partly historical. Many developing countries were newly independent and wanted to assert their sovereignty/ independence and equality with other members states, while the older states took their sovereignty/independence for granted and spoke of them as a matter of course.[25]

The origin and development of the principle of permanent sovereignty over natural resources can be divided into four phases.[26] During the first phase, that is, from 1952 till the adoption of resolution 1803 (XVII) of 14 December 1962, the United Nations was pre-occupied with the formulation of the right of peoples to use and exploit their natural resources as a right inherent in their sovereignty.[27] The most important resolution passed during this phase was the Declaration on Permanent Sovereignty Over Natural Resources,

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[24] *Ibid.* at 144-145.

[25] *Ibid.* at 145.

[26] S.R. Chowdhury, "Permanent Sovereignty Over Natural Resources" in K. Hossain & S.R. Chowdhury eds., *Permanent Sovereignty Over Natural Resources in International Law* (New York: St. Martin's Press, 1984) at 3.

[27] *Ibid.*

resolution 1803 (XVII) of 14 December 1962, popularly known as the landmark resolution. There were eighty seven votes in favour, two against (France and South Africa) and twelve abstentions (ten socialist countries and two developing countries).[28] The Declaration states, *inter alia*, that "the right of peoples and nations to permanent sovereignty over their natural wealth and resources must be exercised in the interests of their national development and the well-being of the people of the state concerned", that exploitation of resources and import of capital should be in conformity with freely negotiated agreements, that capital and profits thereon should be in terms of authorization by national legislation and by international law; that nationalization and expropriation shall be based on grounds of public utility, security or national interest and on "appropriate" compensation in accordance with national legislation of the country nationalizing and in accordance with international law.[29] This Declaration finally settled the debate between the developing and developed countries. It rejected the claim for an unlimited sovereignty, but recognized the right of a state to nationalize property subject to the payment of "appropriate" compensation.

The importance of this resolution lies in the fact that it received the support of the developed and developing countries.[30] The resolution represents a compromise between the interests of developing countries in the protection of their rights over their natural wealth and resources and those of the developed countries in securing adequate guarantees for the protection of foreign investments.[31] It is the last resolution which explicitly recognizes, within this context, the relevance of international law for the protection of foreign investment.[32] It contains both the traditional norms of international law relating to the protection of foreign investment as well as the new norm of permanent sovereignty over natural resources.[33]

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[28] Rajan, *supra*, note 11 at 20.

[29] *Ibid*. at 20-21.

[30] Sornarajah, *supra*, note 6 at 121.

During the second phase, from 1962 to 1973, the landmark resolution was adopted, reiterated and reaffirmed in a number of other resolutions. In resolution 88 (XIII) of 19 October 1972, the Trade and Development Board of the United Nations Conference on Trade and Development (UNCTAD) reaffirmed 'the sovereign right of all countries freely to dispose of their natural resources for the benefit of their national development.' It was specifically provided that this resolution "is without prejudice to what is set forth in General Assembly resolution 1803." Other resolutions adopted during this period included, *inter alia*, resolutions 2158 (XXI) of 1966, 2692 (XXV) of 1970 and 3171 (XXVIII) of 1973.[34] These resolutions prepared the ground for the culmination of these developments in the context of the New International Economic Order (NIEO).[35]

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[31] *Ibid.*

[32] Kemper, *supra*, note 7 at 30.

[33] Sornarajah, *supra*, note 6 at 122.

[34] Chowdhury, *supra*, note 26 at 3-4.

The third phase relates to the incorporation of the principle of permanent sovereignty over natural resources in the Declaration on the Establishment of a New International Economic Order, resolution 3021 (S-VI) of May 1 1974 and *Article* 2 of the Charter of Economic Rights and Duties of States (CERDS) which was adopted by the General Assembly in resolution 3281 (XXIX) of 12 December 1974.[36] A serious dispute arose about the consistency of some of the pertinent provisions of the NIEO and the CERDS with the standards of customary international law, particularly the standards recognized in resolution 1803 relating to the protection of foreign investment.[37] It has been argued that these resolutions undermine resolution 1803 which has sought to incorporate existing international law norms as factors limiting the scope of the principle of permanent sovereignty over natural resources.[38] It has, therefore, been concluded that these resolutions free the principle of permanent sovereignty from the limitations set upon it by resolution 1803.[39]

During the fourth phase, several investment agreements concluded by some developing countries, particularly the oil exporters, went through a series of amendments in order to bring them in line with the principle of permanent sovereignty over natural resources. This process is examined below.

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[35] Kemper, *supra*, note 7 at 30-31.

[36] Chowdhury, *supra*, note 26 at 2.

[37] *Ibid*. at 5. See also Kemper, *supra*, note 7 at 31.

[38] Sornarajah, *supra*, note 6 at 123.

[39] *Ibid*.

4.2. The Legal Status of the Resolutions

There is a divergence of legal opinion as to the precise legal status of the resolutions on permanent sovereignty over natural resources. On this issue, there are two schools of thought. The first school of thought is held by the developing countries and is succinctly described by Chowdhury:[40]

> The right of permanent sovereignty, emanating as it does from the right to self-determination, has the same status of *jus cogens* in contemporary international law. Consequently, the exercise of such right is not defeasible by treaty or by contract. This position is not affected by the fact that there is still difference of opinion with regard to the legal status of some of the corollary rights flowing from the peremptory principle of permanent sovereignty.

The developing countries regard the principle of permanent sovereignty over natural resources as inalienable; as a rule of *ius cogens*, a norm accepted and recognized by the international community of states as a whole and from which no derogation is permitted unless by a subsequent norm of general international law having the same character.[41] The effect of this proposition put forward by the developing countries is that foreign investment agreements which are inconsistent with the principle of permanent sovereignty over natural resources would lose validity in law.[42]

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[40] *Supra*, note 26 at 38. A similar view is also expressed by Sornarajah, *supra*, note 6 at 120-121 and Elian, *supra*, note 14 at 95. See also M. Sornarajah, "The Myth of International Contract Law" (1982) 16 J.W.T.L. 187 at 208, where the writer said: "It is well accepted among, public international lawyers that the principle of self-determination is now a part of public international law. The recognition of the economic counterpart of that principle, the principle of permanent sovereignty over natural resources, has gone through the same process of creation and developed in the same climate of decolonization . The latter principle must be accorded the same status in international law as the principle of self-determination."

[41] D. Flint, "Foreign Investment and the New International Economic Order" in K. Hossain & S.R. Chowdhury eds., *supra*, note 26 at 158. Writers who support this view include; Elian, *ibid*. at 10-11 and Judge Jimenez de Arechaga, (1978) 1 *Recueil des cours* at 297 referred to in I. Brownlie, (1979) 1 *Recueil des cours* 253 at 269, where Judge Arechaga said that: "The

However, the argument that the principle of permanent sovereignty has received acceptance in the world community as *ius cogens* has been resisted particularly by the developed countries who advance the second school of thought.[43] It is argued by these countries that, although resolution 1803 enjoyed the support of developed and developing countries, the resolution in itself does not create public international law.[44] The developed countries regard resolution 1803 as expressing an *opinio juris communis*, and declaratory of existing principles of international law. The same cannot, however, be said of the resolutions on the NIEO and the CERDS. These resolutions appear to contradict resolution 1803, in that reference to international law rules relating to the protection of foreign investment is omitted.

In *Texaco Petroleum Development Company and California Asiatic*

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territorial state can never lose its legal capacity to change the destination or the method of exploitation of those resources, whatever arrangements have been made for their exploitation and administration, even if a predecessor state or a previous government engaged itself, by treaty or by a contract, not to do so." The same views are also expressed by Arechaga in his paper "Application of the Rules of State Responsibility to the Nationalization of Foreign Owned Property", in K. Hossain ed., *Legal Aspects of the New International Economic Order* (New York: Frances Pinter (Publishers) Ltd., 1980) at 220-233.

[42] Sornarajah, *supra*, note 6 at 126.

[43] *Ibid*.

[44] Flint, *supra*, note 41 at 157-158.

Company v. *Libya*,[45] the sole arbitrator, Professor Dupuy, rejected the resolutions on the NIEO and the CERDS as having any law creating effect. He regarded them as essentially *de lege ferenda*, and considered that they have validity "only in the eyes of the states which have adopted them."[46] This was because, unlike resolution 1803, they did not have the support of the developed countries, and in the view of Professor Dupuy, they purported to modify existing principles of international law.[47] A similar view was expressed by the arbitrators in *American Independent Oil Company* v. *The Government of Kuwait*.[48] The arbitrators said:[49]

> On the public international law plane it has been claimed that permanent sovereignty over natural resources has become an imperative rule of *ius cogens* prohibiting states from affording by contract or by treaty, guarantees of any kind against the exercise of the public authority in regard to all matters relating to natural riches. *This contention lacks all foundation. Even if Assembly resolution 1803 (XVII), adopted in 1962, is to be regarded, by reason of the circumstances of its adoption, as reflecting the then state of international law, such is not the case with subsequent resolutions which have not had the same degree of authority....*
>
> (Emphasis is mine).

Although it is generally accepted that resolutions of the General Assembly are not legally binding, this is not to say that they are without legal effect whatsoever.[50] Whatever may be the content of the recommendation and the circumstances of the majority by which it has been reached, it is nevertheless a legal act of the principal organ of the United Nations, whose members are under a duty to treat with some degree of respect.[51] It is submitted that, despite the divergence of legal opinion as to the legal status of the resolutions on the NIEO and CERDS, some of the principles laid down in the resolutions undoubtedly represent recognized legal norms under existing international law, while others indicate emerging norms or directory principles relating to economic relations.[52] It has also been contended that, assuming that this argument contesting the law creating force of the resolutions is valid, it nevertheless loses force because the principle of permanent sovereignty has been acted upon so consistently that it has become a principle of international law through state practice.[53] This argument has some merit. The adoption of the principle can be seen in national legislation, in constitutional provisions and in the new types of foreign investment agreements.[54] It is submitted that if an IOC enters into a contract with a HC, with the knowledge of the existence of a provision asserting the HC's permanent sovereignty over its natural resources and the power to unilaterally alter the contract, there is no reason why it should not be bound by the contract.

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[45] (1979) 53 I.L.R. 389.

[46] Sornarajah, *supra*, note 6 at 128.

[47] Flint, *supra*, note 41 at 158.

[48] (1982) 21 I.L.M. 976.

[49] *Ibid.* at 1021-1022.

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[50] P.J. O'Keefe, "The United Nations and Permanent Sovereignty Over Natural Resources" (1974) 8 J.W.T.L. 239 at 249.

[51] Sir Hersch Lauterpacht, South West Africa - voting procedure, Advisory opinion of June 7th, 1955: I.C.J. Reports, 1955 67 at 120. See also Rajan, *supra*, note 11 at 130 and Brownlie, *supra*, note 41 at 260, where the author said: "The fact that in principle resolutions as a class are not binding has led to no little confusion and it is sometimes said that General Assembly resolutions 'have no legislative effect'. In one sense this is correct: as such the resolutions do not make new law. However, if it is inferred that such resolutions can have no effect on the shaping of international law this is a capital error. The circumstances in which a particular resolution is adopted, the statements of delegations in the debate, the voting, the explanation of votes and the content of the resolution itself, are all indicators of the *evidential* significance of the individual resolution. The key to the problem is the fact that the proceedings of the General Assembly, as of any international conference, are a vehicle for the formulation and expression of the practice of States in matters pertaining to international law. Thus the proceedings and the resolution themselves, constitute *evidence* of the formation of rules of customary (or general) international law."

[52] Chowdhury, *supra*, note 26 at 6.

Even if it is accepted that the General Assembly resolutions only succeeded in creating a weak norm its continued acceptance by many states, in their practices relating to investment agreements, converts it into a principle of customary international law.[55] Its historical and political links with the principle of self-determination may establish permanent sovereignty over natural resources as a part of *ius cogens*, even if this evolution has not already taken place.[56] In the next section, we shall examine the contribution of the principle and its compatibilty with the modes of acquisition of oil rights.

4.3. The Contribution of the Principle and its Compatibility with the Modes of Acquisition of Oil Rights

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[53] Sornarajah, *supra*, note 6 at 129.

[54] *Ibid*. See for example, section 40(3) of the *Federal Constitution of Nigeria* 1979 and section 1(1) of the *Petroleum Act* of 1969, both referred to in section 2.1. of chapter 2. The principle appears not only in the legislation of developing countries which have subscribe to the formation of the principle, but also in the laws of developed countries. See Sornarajah, *supra*, note 40 at 211.

[55] Sornarajah, *supra*, note 6 at 129.

[56] *Ibid*. at 129-130.

The developments that took place in the modes of acquisition of oil rights in developing countries support the view that the principle of permanent sovereignty over natural resources has been a driving force in the realization of the new modes of acquisition of oil rights. Some developing countries, particularly the petroleum exporters, have made great strides towards translating the norms and principles of the resolutions into a living reality.[57] An examination of the new modes of acquisition of oil rights supports the view that the principle of permanent sovereignty over natural resources provided a basis on which most developing countries claimed to alter inequitable legal arrangements under which foreign investors enjoyed rights to exploit natural resources found within their territories.[58] In Nigeria, the progressive development from the framework of the repealed *Mineral Oils Ordinance* of 1914, which gave to the IOCs concession rights over vast areas of the country, to equity participation and contractual joint ventures, described in chapters two and three respectively, attest to the fact that the principle had an impact on the modes of acquisition of oil rights in Nigeria.

The declarations contained in the principle provided guidelines which assisted developing countries to proceed to establish new modes of acquisition of oil rights and represented an improvement on the classical contractual framework of the traditional concessions.[59] The principle has, thus, proved to be a seminal source for rules from which states have derived a wide range of powers aimed at securing effective control over their natural resources and maximizing benefits from their exploitation.[60] The principle also recognizes the overriding powers of the state to dispose of its natural resources in its territory for the benefit of its own people.[61] Thus, the principle has been relied upon to invalidate arrangements regarded as incompatible with it, to restructure existing arrangements and to develop new forms of arrangements.[62]

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[57] H.S. Zakariya, "Sovereignty Over Natural Resources and the Search for a New International Order" in K. Hossain ed., *supra*, note 41 at 217.

[58] K. Hossain, "Permanent Sovereignty Over Natural Resources" in K. Hossain ed., *supra*, note 41 at 35.

Since resolution 1803 is widely accepted as declaratory of customary international law, it shall be our basic point of reference. The criteria enunciated in resolution 1803 underline at least three basic requirements which must be met before a legal arrangement can be regarded as compatible with the principle of permanent sovereignty over natural resources. These are:[63]

> (i) It must be in the interest of national development and the well-being of the people of the state concerned;
>
> (ii) it must be in accordance with the national legislation in force; and
>
> (iii) it must be freely entered into.

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[59] *Ibid.*

[60] K. Hossain, "Introduction" in K. Hossain & S.R. Chowdhury eds., *supra*, note 26 at xiii.

[61] *Ibid.*

[62] *Ibid.*

[63] Hossain, *supra*, note 58 at 39.

Although the present modes of acquisition of oil rights in Nigeria were inspired by the principle of permanent sovereignty over natural resources, it is necessary to pose the following question: Are the present modes of acquisition of oil rights in Nigeria compatible with the principle ? With respect to the first criterion, it may prove difficult to determine whether a particular framework for oil development is for the advancement of national development and the well-being of the people of the state concerned. This is because several opinions may exist as to whether a particular framework is capable of achieving this requirement.[64] According to Hossain:[65]

> Its application, however, would present little difficulty where a manifestly disadvantageous agreement had been entered into, as for example, in a state where oil is newly discovered, the government agency concerned either in ignorance or due to being unduly influenced by bribery or other forms of illegal inducements, agreed to sell oil at $10 per barrel at a time when the price was over $30 per barrel. Such an agreement, it is submitted, would be voidable at the instance of the state.

Applying the above criterion to the modes of acquisition of oil rights in Nigeria, the following observations can be made. The modes of acquisition of oil rights described in chapters 2 and 3 of this thesis point to the fact that great strides have been made from the framework of the repealed *Mineral Oils Ordinance* of 1914. However, it should be appreciated that "*ultimately, it is mainly through the development of national capabilities to undertake and conduct operations that a state can expect effectively to exercise its*

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[64] *Ibid.*

[65] *Ibid.*

sovereignty over natural resources."[66] The lack of technological capability to effectively control the oil industry calls into question whether the present modes of acquisition of oil rights is in the interest of national development and the well-being of the people of Nigeria. A country that cannot boast of exercising *de facto* control of its oil industry can hardly lay claim to permanent sovereignty over its oil resources.

As regards the second criterion, it has been argued that a legal mechanism by which permanent sovereignty over natural resources can be secured is through the exercise of legislative powers to modify natural resources development arrangements.[67] In Alberta, this can be done, as we have seen earlier in chapter 3, under the *change of law clause* which can be found in leases and licences granted by the Crown. Similarly, it is specifically provided in contractual arrangements in Nigeria that these contracts do not prevent the government of Nigeria from exercising its inalienable rights. Where such an alteration occurs, the party adversely affected is not entitled to any compensation, since the original agreement had expressly subjected the terms and conditions to modification by subsequent legislation.[68]

Finally on the third criterion, it is a generally accepted principle of the law of contract that the absence of free consent by either of the parties to an agreement is capable of vitiating the contract. Free consent in that context is understood as consent which is not caused by coercion, undue influence, fraud, misrepresentation or mistake.[69] Thus, the presence of any of the above elements in a natural resources development agreement, would render such an agreement void or voidable.[70] It may even be argued that the possession of a high degree of expertise, coupled with the information at its disposal, imposes a duty of *uberrimae fidei* on the foreign investor and a failure to disclose a material fact which is later discovered, and which if known might have prevented the government from entering into the agreement, would lead to the agreement been declared void or voidable at the option of the government.[71]

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[66] *Ibid.* at 43. Emphasis is mine.

[67] *Ibid.* at 40.

[68] *Ibid.*

It is doubtful that this argument will be upheld by a tribunal. It is, therefore, a difficult task for the government of a developing country to show that an oil development agreement was not freely entered into. It cannot, however, be disputed that the circumstances under which the traditional concession agreements were entered into belie all the classical theories of freedom of contract.[72] Although, modern contractual arrangements in Nigeria's oil industry were freely entered into, it is doubtful if they can be regarded as being in the interest of national development and the well-being of the people. This is because, the country under the existing modes of acquisition of oil rights, has not developed the technological and managerial capabilities so as to be able to exercise *de facto* control of the oil industry. National development can only be achieved through the development of the technological capabilities in the oil industry.

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[69] *Ibid.* at 41.

[70] *Ibid.*

[71] *Ibid.*

[72] S.K.B. Asante, "Stability of Contractual Relations in the Transnational Investment Process" (1979) 28 I.C.L.Q. 401 at 408.

4.4. An Assessment

In order to assess the impact of the principle of permanent sovereignty over natural resources on the modes of acquisition of oil rights, the circumstances under which it was negotiated must be taken into consideration. Having been negotiated within the United Nations framework, it represented an attempt to reconcile the competing, and in some respects conflicting interests of developing countries - the owners of the natural resources - and developed countries - the home country of the foreign investors, holding concession rights to exploit those resources in the developing countries.[73] Since the adoption of resolution 1803, oil development agreements have been subjected to extensive review.[74] States have invoked the principle of permanent sovereignty over natural resources to repudiate agreements or to alter certain terms which are regarded as incompatible with the principle.[75]

The signposts provided by the Declaration, and later by OPEC in its

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[73] Hossain, *supra*, note 58 at 35.

[74] *Ibid*. at 41.

[75] *Ibid*.

Declaratory Statement of Petroleum Policy in 1968,[76] led to the evolution of new types of arrangements, such as equity participation and contractual joint ventures. From the HC's point of view, this development marked significant improvements over the traditional concession, under which the state granted rights over vast expanses of territory, for long durations, reserving for itself only a modest financial payment.[77]

It cannot be denied that these resolutions were, for oil exporting developing countries, a rich source of inspiration.[78] Without these resolutions, which helped to shift the bargaining power from the IOCs to the HCs, it would have been more difficult to realize such basic objectives, as for example, the equitable sharing of benefits, state participation in the oil industry and renegotiation and readjustment of terms in light of changed circumstances.[79] As Nigeria and other oil exporting developing countries seek to acquire the technological and managerial skills so as to be able to control operations directly, more changes are likely to occur in the oil industry. Solutions in this vast and complex field of international economic relations, if they are to last and be successful, require the co-operation of all the parties involved.[80] The overall goal therefore, must be to reach reasonable arrangements in each individual case for the HC and the IOC alike - securing the legitimate political, social and economic goals of the HC without frustrating the reasonable expectations of the IOC.[81]

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[76] *OPEC Resolutions and Official Press Releases* 1960-1990.

[77] Hossain, *supra*, note 58 at 42. See also section 1.3. of chapter 1.

[78] Zakariya, *supra*, note 57 at 210.

[79] *Ibid*. See also Baloro, *supra*, note 4 at 338.

[80] Kemper, *supra*, note 7 at 34.

4.5. Conclusion

The generic principle of permanent sovereignty thus finds a specific expression in the law of permanent sovereignty over natural resources, which is a part of international law rules governing transnational economic co-operation.[82] It was the restoration of political sovereignty to a large number of formerly dependent nations and peoples that gave a strong impetus to the age-old struggle for a just international economic order.[83] These newly independent states found that many of the legal arrangements entered into during the colonial period with foreign investors, exploring their natural wealth and resources, were unfair, inequitable and detrimental to the interests of the people themselves who were the owners of those resources.[84] It was, therefore, the quest for economic independence that gave birth to the principle of permanent sovereignty over natural resources.

It has further been argued, that the principle of permanent sovereignty over natural resources embraces the concept of "mutual equivalence of contractual advantages" as its basic jurisprudential content and seeks to maintain such equivalence by providing rules for redressing gross inequality in bargaining position due to economic compulsion at the time of signing the concession contracts.[85] This principle, will continue to be a driving force in the ever changing relationship between the oil exporting developing countries and the IOCs. Ultimately, unless Nigeria and other oil exporting developing countries develope or acquire the technological capabilities for running operations in the oil industry directly, permanent sovereignty cannot be fully attained.

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[81] *Ibid.*

[82] M. Mughraby, *Permanent Sovereignty Over Oil Resources* (Beirut: Middle East Publishing Centre, 1966) at 161.

[83] C. Theodoropoulos & Y. Omorogbe, "The Role of Arbitration in the Settlement of Oil Investment Disputes." Paper presented at the National Workshop on Petroleum Law, held at the University of Lagos, Lagos, May 28 - June 2, 1984.

[84] Chowdhury, *supra*, note 25 at 1.

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[85] Mughraby, *supra*, note 81 at 161.

Chapter 5

5.0. General Conclusion and Recommendations

This thesis has shown that despite the shortcomings concerning equity participation, production sharing and service contracts, which comprise the heart of this thesis, some progress has been made in Nigeria's oil industry within the past twenty years. Indeed, one can see, in a number of areas, significant gains during this period. For example, the decade of the 1970s witnessed a number of significant advances by the Nigerian government in acquiring majority shares in the subsidiaries of the IOCs, thereby increasing its revenue from the oil industry. But as more is learned about the role of oil in the economic development of Nigeria, the less certain it is that the major problems have, in fact, been solved.[1] It appears that the gains of the last twenty years have merely provided the foundation for coming to terms with the issues that are likely to have an impact on the economic, social and political development of Nigeria.[2]

The gravamen of this thesis has been that, notwithstanding the changes which took place in Nigeria's oil industry within the past twenty years, *de facto* control is still in the hands of the IOCs. At present the government's participation in the oil industry is visibly limited to profit sharing.[3] Such areas as operational policies of the subsidiary oil companies are still in the hands of the management of these companies, which are controlled by their parent companies in Europe or America. If the objectives of the government are to be achieved, the government must establish itself effectively in the oil industry. For this to be accomplished, the government must go beyond majority shareholding and actually secure *de facto* control of the operational policies of the subsidiary oil companies. This could be done through the setting up of effective management committees to run the affairs of the oil companies with the government's interest properly protected.[4] From such a vantage point, the government can easily influence the operational policies of the subsidiary oil companies and ensure their compatibility with the government's overall objectives. This would extend the government's interest in the oil industry beyond that of revenue maximisation to that of developing or acquiring the technology that would enable it to exercise control of its oil industry. The IOC's main objective is to make profit. This objective may conflict with the government's objective of developing or acquiring the technology necessary for running its oil industry.

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[1] D.N. Smith, *New Eyes for Old: The Future, Present and Past in the Evolution of Mineral Agreements* (Lagos: The Nigerian Institute of Advanced Legal Studies, 1981) at 6.

[2] *Ibid.*

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[3] S.B. Falegan & G.O. Okah, "The Contribution of Petroleum to the Nigerian Economy" in *Oil and the New International Economic Order*, Proceedings of the Annual Conference of the Nigerian Economic Society (Ibadan: The Nigerian Economic Society, 1976), 163 at 184.

[4] *Ibid*. It is disturbing to note that it was in 1991 that the NNPC signed its first joint operating agreement (JOA) with an IOC. Under a JOA, a management committee comprising representatives of the joint venture partners is set up. See the JOA between the joint venture partners in the NNPC/Shell joint ventures, referred to in section 2.3.b. of chapter 2.

The government must also have its own pool of qualified Nigerian personnel that will translate its policies and objectives into practical reality. Already, the training of high and medium level manpower, both locally and abroad, is being undertaken by the government.[5] This, together with the formulation of a clear oil policy to guide management, would enable the government to exercise *de facto* control of the oil industry.

In addition, this thesis has shown that, although it is attractive to think about the modes of acquisition of oil rights along a spectrum running from the traditional concession under the repealed *Mineral Oils Ordinance* of 1914 to equity participation, and then to production sharing and service contracts, there is no reason to believe that such a movement leads to *de facto* control of the oil industry by Nigerians.[6] In each one of these new modes of acquisition of oil rights, the old problem of the absence of real control of the oil industry by Nigerians remains. The tendency to look at the evolution of the modes of acquisition of oil rights in the context of structure is, therefore, highly misleading and largely counter-productive.[7] It has also been argued that oil agreements must no longer be viewed simply as contracts, but also as economic development agreements. Economic development agreements provide an avenue for the training of Nigerians in petroleum technology and, thus, may enable the creation of the vital ingredients for the attainment of *de facto* control of the oil industry.

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[5] Falegan & Okah, *ibid*.

[6] Smith, *supra*, note 1 at 17. See also R. Synge, "Change in the Pipeline ?" (1991) September/October, South Magazine at 61, where the writer submits that: "But very little has changed in the oil industry since the early 1970s...."

[7] Smith, *ibid*.

It is also clear that sharing representation at the board of directors of the subsidiary oil companies does not ensure *de facto* control, nor does majority shareholding. The government has generally failed to articulate clearly what it means by "control" as provided in section 1(1) of the *Petroleum Act* of 1969. The problem of *de facto* control by Nigerians of the oil industry will persist until there is a clearer articulation and implementation of the government's objectives. The evolution of the modes of acquisition of oil rights from the traditional concessions to contractual joint ventures reflected the movement from the old international economic order of investor ownership and control of a state's natural resources. Under the new international economic order, the ownership and control of natural resources by host countries was recognized by the international community of states. Despite this development, there has been a confusion of symbols and substance by the government. Although the conferral of ownership and control of oil resources on the government is a marked departure from the traditional concession, the government is still divested of effective powers of control because it has transferred extensive powers of management to the IOCs. The old international economic order which prevailed under colonial rule continues to persist into the post-independence era and has, thus, thwarted the main objective of the principle of permanent sovereignty over natural resources. Since ownership and control (*de facto* control) are synonymous with sovereignty, it is submitted that a country that cannot boast of controlling its oil industry can hardly lay claim to permanent sovereignty over its oil resources.

It has also been shown that in the absence of *de facto* control of the oil industry by Nigerians, the present modes of acquisition of oil rights by the IOCs, are not for the benefit of national development and the well-being of the people of Nigeria. In light of the above, it has been suggested that in order for the government to fully achieve permanent sovereignty over its oil resources, it should nationalize the oil industry [8] or encourage indigenous participation in the exploration and production of oil. I will briefly examine these two alternatives.

5.1. Nationalization of the Oil Industry

Nationalization of the oil industry is a relatively easy step for host countries to take in an attempt to oust the IOCs from their position of dominance of the host country's oil industry. It can hardly be denied that nationalization definitively settles the issue of ownership.[9] Nationalization transfers the full ownership of the oil industry to the government. However, the bare assertion of state ownership does not dispose of all the incidence of the IOC's *de facto* control of the oil industry.

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[8] P.C. Asiodu, "Comments and Criticisms of Evolution of Nigerian Oil Policy by M.O. Lolomari" in *Oil and the New International Economic Order, supra*, note 3 at 31.

[9] S.K.B. Asante, "Restructuring Transnational Mineral Agreements" (1979) 73 I.C.L.Q. 335 at 341.

Given the realities of the world oil industry, the experiences of OPEC countries that have nationalized their oil industries and the level of Nigeria's indigenous know-how, the deliberate and progressive manner in which the government has moved from the traditional concessions to joint ventures was realistic.[10] This writer firmly believes that in the absence of skilled Nigerian personnel and the technological capability to run the oil industry, nationalization would not have resulted in *de facto* control of the oil industry by Nigerians.

Furthermore, a comparative study of the oil industry in some OPEC countries shows that nationalization was usually influenced by political motives without adequate consideration of how *de facto* control could have been achieved.[11] Even after nationalization of the oil industry in these OPEC countries, the IOCs continue to exercise real control because of their control of the management of the subsidiary oil companies. This state of affairs calls into question the effectiveness of nationalization as a means of achieving *de facto* control of the oil industry. *De facto* control by Nigerians of the oil industry can only be achieved after a careful consideration of the existing manpower and technological capabilities of the country.

5.2. The Role of Indigenous Oil Companies in the Exploration and Production of Oil in Nigeria

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[10] Asiodu, *supra*, note 8 at 31.

[11] See for example, the nationalization of British Petroleum by the Nigerian government in 1979, referred to in section 2.3. of chapter 2. Other examples include the nationalization of the Anglo-Iranian Oil Company by the Iranian government in 1951 and the nationalization of British Petroleum and Texaco by the Libyan government in 1973.

The question has also been raised as to whether indigenous participation in the exploration and production of oil would have achieved *de facto* control of the oil industry by Nigerians.[12] The exploration and production of oil calls for heavy investments in both capital and a skilled workforce. As a result, getting local investors to go into the oil business has not been an easy affair. In fact, earlier attempts between 1968 and 1987 did not prove successful.[13] Although several oil prospecting licences were granted to indigenous oil companies, some of these companies sold off their licences to foreign oil companies as soon as they were given for reasons not unrelated to the huge financial outlay, high technological and manpower requirements. This has led one writer to conclude that:[14]

> The average Nigerian is content to serve as a mere agent for foreign companies whether in the field of concession awards or in buying crude oil. He is satisfied with being a silent partner waiting for the dividends to *slop, slop, slop into the barrel*, or prostituting concessions for the highest foreign bidder. Nigerians potentially of the stature of Rockefeller, Getty, Mattei or Hammer are not yet on the oil horizon.

In addition, the oil business is capital intensive and sometimes requires a considerably long gestation period. Consequently, it is not easy for indigenous oil companies to convince financial institutions to come to their aid because of the high level of risk involved in exploring for oil.

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[12] M.O. Lolomari, "The Evolution of Nigerian Oil Policy" in *Oil and the New International Economic Order supra*, note 3 at 23.

[13] S. Akinrinade, "Nigeria's Oil Tycoons" (1992) February 17, Newswatch Magazine 22 at 23-24.

[14] Lolomari, *supra*, note 12 at 23.

Recent developments may, however, lead to a change in the dominant role played by the IOCs in Nigeria's oil industry. With the introduction by the government of an accelerated programme of indigenous participation in all aspects of the oil industry, especially exploration and production, we may begin to witness a more active role by Nigerians in the oil industry.[15] To this end, between fourteen and seventeen indigenous companies have been given oil prospecting licences.[16] However, the greatest challenge for the indigenous oil companies, remains how to tackle the financial constraints imposed by the industry. It has been suggested that joint venture financing, involving two or more investors sharing the cost of exploration; or consortium financing, an arrangement that may involve a group of not less than three institutions, including banks, insurance companies, financial houses and other institutional investors could alleviate some of the financial burden placed on indigenous oil companies.[17] Other options available include; the debenture/public issue option, which involves the investor's bank going to the capital market for funds by inviting the general public to invest in the venture in anticipation of the higher yields at maturity. Some other experts are of the opinion that the NNPC could have an important role to play in aiding the indigenous oil companies. It is argued that, apart from tax incentives, the NNPC could enter into joint venture agreements with the indigenous oil companies if oil is found in commercial quantities as it has done with the IOCs.[18]

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[15] Akinrinade, *supra*, note 13 at 26. The former Minister of Petroleum Resources, Professor Jubril Aminu has recently stressed that it is a priority of policy to give Nigerians "every opportunity to participate in the oil industry" and to "indigenise the industry and make it a people's industry", referred to in Synge, *supra*, note 6 at 61. This new government policy has been described as "the most important strategic policy ever made by any Nigerian administration". See M. Adenuga Jnr., "Trends in the Oil Industry: Looking to the Future" (1992) May 4-10 West Africa Magazine at 752.

[16] Akinrinade, *ibid*. Some of these companies include; Cemac Nigeria Limited, Consolidated Oil Limited, Dantata Investments and Securities Company Limited, Queens Petroleum, Summit Oil, Moncref Oil, Paclantic Oil, Cavendish Petroleum, Express Petroleum and Inko Petroleum.

[17] Akinrinade, *ibid*.

The recent discovery of crude oil by Consolidated Oil, an indigenous oil company working offshore, lends credence to the fact that Nigerians given the tools and required resources can work in the upstream and downstream sector of the oil industry. This development, together with the training and employment of qualified Nigerian personnel into key management positions of the IOCs, may in the long run secure for the government the *de facto* control of the oil industry that has eluded it since the discovery of oil in Nigeria in 1956.[19] Even in the face of a variety of new modes of acquisition of oil rights in Nigeria, the IOCs continue to play a dominant role in Nigeria's oil industry.

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[18] *Ibid*. at 22-24.

[19] See however, Synge, *supra*, note 6 at 61, where the writer concludes that the emergence of indigenous oil companies is unlikely to undermine the dominant role of the IOCs in Nigeria's oil industry.

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(2) Faculty of Law, University of Benin, Benin City. Lecturer in Law. 1988 - to date.

(3) Alegeh, Atsegbua & Ossai, Earlham Hall Chambers, Legal Practitioners - Partner (1988 - to date).

AWARD:

(1) The Honourable N.D. McDermid Scholarship in Law from the Faculty of Law, University of Alberta.

CONFERENCES AND SEMINARS ATTENDED:

(i) Nigerian Law Teachers Conference, May 1989, Enugu, Nigeria.

(ii) Nigerian Law Teachers Conference, May 1990, Ibadan, Nigeria.

(iii) Nigerian Bar Association Conference, August 1990, Benin, Nigeria.

(iv) Seminar on Copyright Law, 1990, Benin City, Nigeria.

(v) Nigerian Law Teachers Conference, May 1991, Kano, Nigeria.

(vi) Seminar on Corporate and Investment Law, June

1991, Benin City, Nigeria.

PAPERS PRESENTED AT SEMINAR:

(i) The Legal Framework for Foreign Capital Investment in Nigeria (1991). Presented at the Seminar on Corporate and Investment Law in Nigeria.

MEMBERSHIP OF PROFESSIONAL BODIES:

(i) Member, Nigerian Bar Association (NBA).

(ii) Member, Nigerian Association of Law Teachers (NALT).

UNPUBLISHED PAPERS:

(i) Tort Law and Economics - A Comparative Analysis.

(ii) The Anton Pillar Order and the Protection of Intellectual Property.

(iii) Exemplary Damages in Contract Law - A No Case Submission.

(iv) Constitutional Rights in Nigeria.

PAPERS UNDER CONSIDERATION:

(i) Permanent Sovereignty Over Natural Resources in International Law. (Under consideration by the Indian Law Institute).

(ii) The Acquisition of Oil Rights Under Contractual Joint Ventures in Nigeria. (Under consideration by the Journal of African Law).

(iii) International Arbitration of Oil Investment

Dispute. (Under consideration by Virginia Journal of International Law).

(iv) A Critical Appraisal of Equity Participation in the Nigerian Oil Industry. (Under consideration by OPEC Review).

(v) A Critical Appraisal of the Transfer of Petroleum Technology in the Nigerian Oil Industry. (Under consideration by OPEC Review).

BOOK REVIEW:

(i) The Legal Aspects of Receivables Financing by Fidelis Oditah (London: Sweet & Maxwell, 1991). Reviewed by Lawrence Atsegbua (Forthcoming Journal of Business Law, 1992).